Manual on Concurrent Audit of Banks (2016 Edition)

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Internal Audit Standards Board

The Institute of Chartered Accountants of India

(Set up by an Act of Parliament)

New Delhi

Revised Edition	:	October, 2016
Committee/Department	:	Internal Audit Standards Board
Email	:	cia@icai.in
Website	:	www.icai.org
Price	:	₹ 350/- (*including CD*)
ISBN No.	:	978-81-8441-128-7
Published by	:	The Publication Department on behalf of the Institute of Chartered Accountants of India, ICAI Bhawan, Post Box No. 7100, Indraprastha Marg, New Delhi - 110 002.
Printed by	:	Sahitya Bhawan Publications, Hospital Road, Agra-282 003
		October/2016/P2017(Revised)

Foreword

For a growing and dynamic economy like India, that aspires to be globally competitive, a sound and inclusive banking system is extremely important. The stability of various segments in the economy particularly of the financial sectors is directly or indirectly dependent on the banking sector. Indian banks have modernized their processes, restructured their organisations into business verticals, completed Core Banking Solution implementation and launched several products in both the retail and wholesale banking segments to keep pace with the growing challenges.

This changing landscape and the emphasis on risk management and control function makes the role of concurrent auditors very critical. RBI has revised its 1996 concurrent audit guidelines and issued "Concurrent Audit System in Commercial Banks – Revision of RBI's Guidelines" in July, 2015. These guidelines focus on effective controls, importance of checking high risk transactions and coverage of fraud prone areas. In the light of these new Guidelines, the Internal Audit Standards Board (IASB) of the Institute has thoroughly revised "Manual on Concurrent Audit of Banks (2012 edition)", including the impact of various applicable new/ revised RBI Circulars issued during the period.

I congratulate CA. Mukesh Singh Kushwah, Chairman, CA. Anil S. Bhandari, Vice-Chairman and other members of the Internal Audit Standards Board on issuance of this revised Manual.

I am sure that this revised edition would help the members in discharging their responsibility, as concurrent auditors, in an efficient and effective manner.

September, 9, 2016	**CA. M Devaraja Reddy**
New Delhi	President, ICAI

Preface

Technological innovation, asset quality, capital adequacy, financial inclusion and talent management are some of the key issues facing the Indian banking industry. Banks are facing challenges related to implementation of Core Banking Solutions, compliance with Basel norms, Non-Performing Asset (NPA) management and above all dealing with the ever growing volume and complexity of transactions. These challenges make the role of chartered accountants crucial as they are instrumental in helping the banks to maintain reliability of different processes and timely reporting of lapses and irregularities.

Concurrent audit is essentially a management process integral to the establishment of sound internal accounting functions and effective controls and setting the tone for a vigilance internal audit to preclude the incidence of serious errors and fraudulent manipulations. Reserve Bank of India had issued concurrent audit guidelines in 1996. Since then a number of development have taken place in banking sector and consequentlyRBI has issued revised Concurrent Audit Guidelines in July, 2015.Keeping this in view, the Internal Audit Standards Board has thoroughly revised "Manual on Concurrent Audit of Banks" which had been issued in 2012. Apart from taking impact of abovementioned circular and all other related new circulars/ directions issued by the RBI, the revised Manual also, includes thoroughly updated Checklist for Concurrent Audit. This revised edition includes new chapters on important areas like, Treasury, Forex and Core Banking Solutions. For ready reference, text of all important Master Circulars and Master Directions issued by the RBI, impacting concurrent audit,have been included in the CD. However, it is extremely important that the concurrent auditors should keep themselves updated regarding all relevant internal guidelines/circulars/important references as well as relevant circulars/ directions being issued by the RBI from time to time.

At this juncture, I wish to place on record my sincere thanks to all the members of the Study Group formed under my convenorship at Delhi, *viz.*, CA. Rakesh Garg (co-convener), CA. Sanjay Gupta, CA. Naresh Gupta, CA. Anil Aggarwal, CA. Anu Pandey, CA. Sandeep Goel, CA. Yogesh Malik and CA. Kapil Chatwal for taking time out of their pressing preoccupations and comprehensively revising and updating this Manual.I would also like to express my gratitude to CA. Shriniwas Y. Joshi, Shri Govadda Subba Rao, Shri P. T. S. Murthy, CA. Kuntal P. Shah, CA. Sachin Ambekar, CA. Tushar Kanti Basu, CA. Anagha Thatte, CA. Vinod Karandikar, CA. Sanjay V. Shah, CA. Dhananjay J. Gokhale, Shri V. Somasekhar, CA. Ramesh A. Shetty and CA. S. Dhayanidhi for providing important support to the group.

The Study Group members were deeply concerned with the expanded scope of work of concurrent audit which may not so strictly fall within the ambit of concurrent audit, and also the remuneration which is not commensurate with the work load of concurrent auditors. Further, it was felt that for good governance and effective implementation of RBI Circulars, the banks should adopt uniform reporting format for concurrent audit, and also review requirement of compulsory attendance by certain banks.

I would also like to thank to CA. M. Devaraja Reddy, President, ICAI and CA. Nilesh Shivji Vikamsey, Vice President, ICAI for their continuous support and encouragement to the initiatives of the Board. I must also thank my colleagues from the Council at the Internal Audit Standards Board, *viz.*, CA. Anil Satyanarayan Bhandari, Vice- Chairman, IASB, CA. Tarun Jamnadas Ghia, CA. Mangesh Pandurang Kinare, CA. Dhinal Ashvinbhai Shah, CA. Babu Abraham Kallivayalil, CA. K. Sripriya, CA. M. P. Vijay Kumar, CA. Ranjeet Kumar Agarwal, CA. Sushil Kumar Goyal, CA. Debashis Mitra, CA. Shyam Lal Agarwal, CA. Kemisha Soni, CA. Sanjiv Kumar Chaudhary, CA. Sanjay Vasudeva and Shri Vithayathil Kurian for their vision and support. I also wish to place on record my gratitude for the co-opted members on the Board *viz.*, CA. Anil Kumar Jain, CA. Kartik Bharatkumar Radia, CA. Krishna Kumar T., CA. Vipin Gupta, CA. Vishwanath K., CA. Yashwant Jaywant Kasar and special invitee *viz.*, CA. Shobhit Dwivedi for their invaluable guidance as also their dedication and support to the various initiatives of the Board. I also wish to express my sincere appreciation for CA. Jyoti Singh, Secretary, IASB and her team for their efforts in revising this Manual.

I am sure that the members and other interested readers would find this revised Manual immensely useful.

October 13, 2016
New Delhi

CA. Mukesh Singh Kushwah
Chairman
Internal Audit Standards Board

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PART I

Understanding the Banking Business and Its Legal Framework

Chapter 1
Banking in India

Evolution of the Banking Institution in India

1.1 Banking on modern lines started with the establishment of banks by the English Agency Houses at Kolkata and Bombay. Bank of Hindustan, the first Bank in India on modern line was established in 1770. Bank of Bengal was established in 1786 at Kolkata. Subsequently, three presidency banks were established in Kolkata (1806), in Mumbai (1840) and in Chennai (1843). In early years, these presidency banks were allowed to issue currency notes until 1862 when the Government started issuing currency notes. Moreover, in the year 1860, the concept of limited liability for banks was accepted under Indian Law.

1.2 Till 1860, the banks, which were in existence, opened branches in various cities and towns like Agra, Mumbai, Chennai, Banaras, Simla, and Delhi, etc. By the end of 1900, there were three classes of banks in India *viz*. the Presidency Banks (which were three in number); the Joint Sector Banks (nine in number); and Exchange Banks or Foreign Banks (eight in number). Some of the prominent joint sector banks were the Allahabad Bank, the Alliance Bank of Simla, the Oudh Bank and the Punjab National Bank.

1.3 **1900-1950:** The *Swadeshi* movement, which started in the early phase of 1900s, gave stimulus to growth of banking system in India. It resulted in establishment of joint stock banks by Indians. The more prominent of them were the Peoples' Bank of India; the Bank of India; the Bank of Baroda; the Central Bank of India, etc. During this period, Indian Joint Stock Banks, specializing in short term credit for trade in the form of cash credit and overdraft, started operation. The Indian banks did not undertake foreign exchange business, and the monopoly remained with foreign banks. In 1921, the Presidency banks were merged and the Imperial Bank of India was created. Subsequently, the same Bank was converted into the State Bank of India. The period of 1900 to 1925, however, saw failure of many banks. The phenomenon attracted attention of the Government of India and acommittee, Central Banking Enquiry Committee, was constituted by the Government in 1929 to trace reasons behind failure of banks. The Committee highlighted some important reasons responsible for bank failures including. insufficient capital, poor liquidity of assets, combination of non-banking activities with banking activities, irrational credit policy, incompetent and inexperienced directors, etc.

1.4 The Reserve Bank of India (RBI) Act was passed in 1934 and the Reserve Bank of India came into existence in 1935 on the basis of major recommendations of Central Banking Enquiry Committee. In 1949, the Banking Regulation Act was passed which gave wide powers to the RBI with regard to establishment of new banks, mergers and amalgamation of banks, opening of new branches, closing of existing branches, shifting of existing branches to other locations, etc., including inspection of banks. The Banking Regulation Act, 1949 gave wide powers to RBI to regulate, supervise and develop the banking system. The period after 1949 was marked by the efforts of RBI towards institutionalization of savings, to adapt the credit system that was suitable to the emerging needs of the economy.

The Banking Regulation Act,1949 was landmark legislation. The Act, thus, provided framework for RBI's supervision of banks. In 1947, India got independence and the partition thereafter affected Indian banking system.

1.5 **1950-1969:** This period in history of banking industry in India was marked by important events including constitution of the State Bank of India (the State Bank of India (SBI) became successor to the Imperial Bank of India under the State Bank of India Act, 1955), the creation of a state partnered/state sponsored Bank, in order to have effective control over the Imperial Bank of India and integrating it with the former state owned banks of princely states. Later, the State Bank of India (Subsidiary Banks) Act was passed in 1959 enabling the SBI to take over eight state-associated banks as its subsidiaries. State Bank of Bikaner and State Bank of Jaipur were merged into one Bank, *viz.* State Bank of Bikaner and Jaipur and the other state owned banks were, the State Bank of Indore, the State Bank of Mysore, the State Bank of Patiala, the State Bank of Saurashtra, the State Bank of Hyderabad, and the State Bank of Travancore. The conversion of Imperial Bank of India into the State Bank of India and the reconstitution of Associate Bank in 1959, were intended to accelerate the pace of extension of banking facilities all over the country.

1.6 **1969-1990:** To bring about a wider diffusion of banking facilities and to change the uneven distribution of pattern of lending, schemes for social control for banks was announced in the Parliament in December 1967, to ensure an equitable and purposive distribution of credit within the resources available, keeping in view the relative priorities of developmental needs. The social control measures were designed to achieve a social orientation of banking within the framework of existing ownership. National Credit Council was set up in 1968 to assess the demand for bank credit from various sectors of the economy and to determine the priorities. In July 1969, the Government of India nationalized 14 major banks, which became one of the important events in the history of Indian Banking. Banks were nationalized to achieve social objectives so that they effectively played the role of catalytic agents for economic growth by extending banking facilities in all parts of the country. Six more Banks were nationalized thereafter termed as "Corresponding New Bank" (the body corporate specified against an existing Bank in column 2 of the First Schedule of Banking Companies Act, 1980). With a view to develop the rural economy with development of agriculture, trade, commerce, industry and all other productive activities in the rural area RRBs were established under the Regional Rural Banks Act, 1976.

Today's Era

1.7 "Report on Trend and Progress of Banking in India 2014-15[1]" issued by the Reserve Bank of India states that the operations of banking sector and the NBFC sector for the year 2014-15, exhibited several week spots. However, when compared with the global banking trends in profitability, asset quality and capital positions, the Indian banking sector did not appear to be an exceptional under-performer. Furthermore, the regulatory steps initiated in 2014-15 as well as in earlier years are expected to address many of short-term concerns afflicting the sector, while paving way for medium to long-term reforms in this sector.

1.8 Some of the major regulatory steps taken during the year and the perspective about how these steps would help in reforming the Indian Banking sector are as follows:

(a) De-stressing the banking sector

(b) Reforming the public sector banks (PSBs)

(c) Improving monetary policy transmission

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1 Refer RBI website for full text of Report.

(d) Strengthening the liquidity standards of banks

(e) Monitoring the build-up of leverage in the banking system

(f) Dealing with the concern of too-big-to-fail

(g) Convergence with the international accounting standards

(h) Minimising the regulatory arbitrage between banks and non-banks

(i) Reviving the licensing and expansion of urban co-operative banks

(j) Making the banking sector more inclusive

1.9 Presently, the following types of banking institutions prevail in India:

- Commercial Banks
- Regional Rural Banks
- Co-Operative Banks
- Development Banks more commonly known as 'term-lending institutions'
- Payment banks
- Small finance banks

Commercial Banks

1.10 Commercial banks are by far the most widespread banking institutions in India. Commercial bank is a financial institution, i.e., authorized by law to receive money from businesses and individuals and lend money to bank. Commercial banks are open to the public and serve individuals institutions businesses and corporations, etc. A commercial bank is also regularized through Reserve bank of India. The major products and services rendered by Commercial Banks are given in Chapter 2.

1.11 A number of commercial banks were nationalized with an attempt to shift the focus of commercial bank lending to a large extent. RBI propagated the concept of lending to priority sector and laid down corresponding guidelines. Every commercial bank is required to provide credit to certain important sectors of the Indian economy.

This inaugurated the era of direct credit flows to specified sectors. The financial inclusion of the under-privileged in the banking system started with the nationalization of Banks. According to RBI directives, the scheduled commercial banks are required to ensure that priority sector advances constitute a prescribed minimum level of net bank credit and that a substantial portion is directed towards the weaker sections of the society.

1.12 Credits provided by the commercial banks are an important driver of national economy. During the post-independence period, a phenomenal growth in industrialization has been possible largely due to enhance credit off-take from banks and financial institutions.

Public Sector and Private Sector Banks

1.13 Commercial banks operating in India can be divided into two categories based on their ownership – public sector banks and private sector banks. However, irrespective of the pattern of ownership, all commercial banks in India function under the overall supervision and control of the RBI.

1.14 Public sector banks comprise the State Bank of India, its five subsidiaries (also called 'associate banks' of State Bank of India; these are State Bank of Bikaner and Jaipur, State Bank of Hyderabad, State Bank of Mysore, State Bank of Patiala, and State Bank of Travancore), IDBI Bank Ltd. and the nationalised banks.

While the majority stake in the Share Capital of all Public Sector Banks is with the Government of India, there are private individual/institutional shareholders also. The majority stake in the share capital of associate banks of State Bank of India has been subscribed to by the parent, i.e., State Bank of India.

1.15 The ownership of private sector banks is with institutional shareholders, private individuals and bodies corporate. Private Sector Banks are of the following types:

(a) Indian scheduled commercial banks other than public sector banks.

These include the 'old' private banks which were in existence before the guidelines for floating new private banks were issued in 1993, the 'new' generation private banks, and the two banks that were granted licenses by RBI in March 2014.

(The term 'scheduled commercial banks' refers to commercial banks which are included in the Second Schedule to the Reserve Bank of India Act, 1934.)

Under Section 2(e) of the RBI Act, a scheduled bank is conferred two main privileges (a) availing of refinance from RBI and (b) permission to participate in the call/notice money market.

It may be noted that all scheduled banks are not commercial banks; some co-operative banks are also scheduled banks. Commonly known as 'banking companies', these banks are 'companies' registered under the Companies Act, 1956 (now the Companies Act, 2013),or an earlier Indian Companies Act.

(b) Non-scheduled banks

(c) Indian branches of banks incorporated outside India, commonly referred to as 'foreign banks'.

Some of the banks have set up subsidiaries – wholly-owned or partly-owned – to operate in some specialised spheres of activity, such as, merchant banking, funds management, housing finance, primary dealership, pension fund management, insurance business, stock broking, credit card activity, factoring, etc. These subsidiaries do not carry on all the principal functions of a commercial bank.

Regional Rural Banks

1.16 These banks have been established "with a view to develop the rural economy by providing, for the purpose of development of agriculture, trade, commerce, industry and other productive activities in the rural areas, credit and other facilities, particularly to the small and marginal farmers, agricultural labourers and artisans and small entrepreneurs. While regional rural banks can carry on any business in which a bank is legally permitted to engage. Section 18 of the Regional Rural Banks Act, 1976, specifically lists the following businesses which such a bank may undertake:

(a) the granting of loans and advances, particularly, to small and marginal farmers and agricultural labourers, whether, individually, or in groups, and to co-operative societies, including agricultural marketing societies, agricultural processing societies, co-operative farming societies, primary agricultural credit societies or farmers' service societies, for agricultural purposes or agricultural operations or for other purposes connected therewith;

(b) the granting of loans and advances, particularly to artisans, small entrepreneurs and persons of small means engaged in trade, commerce or industry or other productive activities, within the notified area in relation to the RRB.

1.17 In order to strengthen and consolidate RRBs, the government in 2005 initiated the process of amalgamation of RRBs in a phased manner. Consequently, the total number of RRBs has reduced from 196 to 56[2]. Further, the Government of India has issued a notification dated May 17, 2007 specifying 'Regional Rural Bank' as 'bank' for the purpose of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002.

1.18 In recent years, in an attempt to strengthen the regional rural banks, several measures have been taken by the Central Government and the RBI. These banks are no longer required to confine their lending to the weaker sections and are permitted to lend to non-target groups also up to specified limits. They can also undertake various types of business, such as, issuance of guarantees, demand drafts, travellers' cheques, etc. Moreover, RRBs are no longer required to confine their operations only within local limits notified by the Central Government; they are now permitted, subject to fulfilling service area obligations, to lend monies outside their service area. In the wake of these developments, the distinction between commercial banks and RRBs has become somewhat blurred.

1.19 Each RRB has a public sector bank as its 'sponsor bank'. Capital in each such bank is contributed by the Central Government, the sponsor bank and the State Government concerned in proportion of 50, 35 and 15 per cent, respectively.

1.20 Apart from subscribing to the share capital of a RRB sponsored by it, the sponsor bank is also required to train personnel of the RRB as also to provide managerial and financial assistance to such bank during the first five years of the latter's functioning (this period can, however, be extended by the Central Government).

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[2] As per the information available from the website of the Reserve Bank of India at the following URL: http://www.rbi.org.in/scripts/AboutUsDisplay.aspx?pg=RegionalRuralBanks.htm.

1.21 Like commercial banks, regional rural banks also function under the overall supervision and control of the RBI. Some of the regulatory functions of the RBI in relation to RRBs have been delegated to the National Bank for Agriculture and Rural Development (NABARD).

Co-operative Banks

1.22 These are banks in the co-operative sector which cater primarily to the credit needs of the farming and allied sectors. Co-operative banks include central co-operative banks, state co-operative banks, primary co-operative banks and land development banks. Of these, primary co-operative banks operate in metropolitan cities, urban and semi-urban centres to cater principally to the credit needs of small industrial units, retail traders, etc. Due to their existence primarily in urban areas, primary co-operative banks are more commonly known as 'Urban Co-operative Banks' (UCB). Land development banks provide long-term finance for agriculture and have a two-tier structure – State Land Development Banks and the Primary Land Development Banks.

1.23 Each co-operative bank operates within a specific geographic jurisdiction as determined by its bye-laws. Co-operative banks can lend monies only to their members or to registered societies. The single most important regulatory and supervisory feature in the co-operative banking sector is the prevalence of dual control. While incorporation/registration and management related activities are regulated in the states by the Registrar of Co-operative Societies or the Central Registrar of Co-operative Societies (for multi-state cooperative banks), banking-related activities are under the regulatory/supervisory purview of the Reserve Bank of India or NABARD (in the case of rural cooperatives).

Foreign Banks

1.24 Foreign banks operate in India through a network of branches and do not have a separate legal entity existence in India. However, the RBI regulates the functioning of these banks in India, with regard to scale and nature of business they undertake in India.

Almost all foreign banks are technologically advanced and use a high level of IT integration into their operations. These systems, in most instances, are similar to those being used by their branches globally. Due to cost-benefit and other considerations, in some instances, foreign banks, get certain financial or other information processed at one of their global centres. This processing of data out of the country is generally with specific consent from the RBI.

1.25 In the aftermath of the global financial crisis and building on the lessons there from, RBI issued a Discussion Paper in January 2011 on the mode of presence of foreign banks in India. Taking into account the feedback received on the Discussion Paper, a Scheme for setting up of locally incorporated Wholly Banking in India Owned Subsidiary (WOS) by foreign banks in India was finalized in November 2013.,

The scheme provided, as hitherto, allowing foreign banks to operate in India either through branch presence or setting up a wholly owned subsidiary (WOS) with near national treatment. The foreign banks in India have to choose one of the above two modes of presence and shall be governed by the principle of single mode of presence. The policy is guided by the two cardinal principles of (i) reciprocity and (ii) single mode of presence. As a locally incorporated bank, the WOS will be given near national treatment which will enable them to open branches anywhere in the country at par with Indian banks (except in certain sensitive areas where RBI's prior approval would be required). They would also be able to participate fully in the development of the Indian financial sector. The policy incentivises the existing foreign bank branches which operate within the framework of India's commitment to the World Trade Organisation (WTO) to convert into WOS due to the attractiveness of near national treatment. Such conversion is also desirable from the financial stability perspective. To provide safeguards against the possibility of the Indian banking system being dominated by foreign banks, the framework has certain measures to contain their expansion if the share of foreign banks exceeds a critical size. Certain measures from corporate governance perspective have also been built in so as to ensure that the public interest is safeguarded.

Payment Banks

1.26 Payment Banks have been introduced in the Indian financial system since November 2014, with the basic objective of furthering financial inclusion by providing (i) small savings accounts and (ii) payments/remittance services to migrant labour workforce, low income households, small businesses, other unorganised sector entities and other users. Their scope of activities includes the acceptance of demand deposits, presently restricted to holding a maximum balance of ₹ one lakh per individual customer, issuance of ATM/debit cards but not credit cards, payments and remittance services through various channels, acting as Business Correspondents (BC) of another bank and distribution of non-risk sharing simple financial products like mutual fund units and insurance products, etc. Payments Banks cannot undertake any lending activities. Apart from amounts maintained as Cash Reserve Ratio (CRR) with RBI on its outside demand and time liabilities, they are required to invest a minimum of 75 per cent of their "demand deposit balances" in Statutory Liquidity Ratio (SLR) eligible Government securities/treasury bills with maturity up to one year and hold maximum 25 per cent in current and time/fixed deposits with other scheduled commercial banks for operational purposes and liquidity management.

Small Finance Banks

1.27 Small Finance Banks have also been introduced in the Indian financial system since November 2014, with the basic objective of furthering financial inclusion by (i) provision of savings vehicles, and (ii) supply of credit to small business units; small and marginal farmers; micro and small industries; and other unorganised sector entities, through high technology-low cost operations. Their scope of activities primarily includes undertaking basic banking activities of acceptance of deposits and lending to unserved and under-served sections including small business units, small and marginal farmers, micro and small industries and unorganised sector entities. There are no restrictions in the area of operations of these banks. The Small Finance Banks are subject to all prudential norms and regulations of RBI as applicable to existing commercial banks including requirement of maintenance of Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR). No forbearance has been provided for complying with the statutory provisions. These banks are required to extend 75 per cent of their Adjusted Net Bank Credit (ANBC) to the sectors eligible for classification as priority sector lending (PSL) by RBI. Also, at least 50 per cent of their loan portfolio should constitute loans and advances of upto ₹ 25 lakh.

Chapter 2
Banking Products and services

Major Products and Services Provided/ Rendered by Commercial Banks

Acceptance of Deposits

2.1 Acceptance of Deposits from the public is one of the most important function of a commercial bank. Commercial banks accept deposits in various forms: term deposits, savings bank deposits, current account deposits, recurring deposit, saving cum term deposit and various others innovative products.

Granting of Advances

2.2 This again is an important function of commercial banks. Advances granted by commercial banks take various forms, such as, cash credit, overdrafts, purchase or discounting of bills, term loans, etc. Apart from granting traditional facilities, banks are also providing facilities like issuance of commercial papers, ECB on behalf of bank/borrower, securitization of receivables, cash overdraft, etc.

Remittances

2.3 This involves transfer of funds from one place to another. Common modes of remittance of funds are drafts and Telegraphic/Mail Transfers (TT/MT) and Electronic Funds Transfer (EFT). Drafts are issued by one branch of the Bank and are payable by another branch of the Bank (or, in case there being no branch of the Bank at the place of destination, branch of another Bank with which the issuing Bank has entered into necessary arrangement). The drafts are handed over to the applicant. In the case of telegraphic/mail transfer, no instrument is handed over to the applicant; the transmission of the instrument is the responsibility of the branch. Generally, the payee of both the TT and the MT is an account holder of the paying branch. In the case of Electronic Fund Transfer,as the name suggest, the funds are transferred electronically between two banks. Common mode of

Electronic Fund Transfer is RTGS (Real Time Gross Settlement) which can be used for remittance of amount of two lakhs or above and NEFT (National Electronic Funds Transfer) which can be used for transfer of any amount. Another mode of EFT service is Immediate Payment Service (IMPS).

Collections

2.4 The customers can lodge various instruments, such as, cheques, drafts, pay orders, travellers cheques, dividend and interest warrants, tax refund orders, etc. drawn in their favour and the trade bills drawn by them on their buyers with their Bank for collection of the amount from the drawee (the bank or the drawer of the bill). They can also lodge their term deposit receipts and other similar instruments with the Bank for collection of the proceeds from the Bank with which the term deposit, etc. is maintained. Banks also collect instruments issued by post offices, like national savings certificates, postal orders, etc.

2.5 The instruments mentioned above may be payable locally or at outside centre. The instruments payable locally are collected through the clearing house mechanism, while the instruments payable outside are sent by the Bank, with which instrument has been lodged, for collection to the branches of the issuing Bank at those centre or, if there is no such branch, to other banks.

Clearing house settles the inter-Bank transactions among the local participating member banks. Generally, post offices are also members of the house. There may be separate clearing houses for MICR (Magnetic Ink Character Recognition) and non-MICR instruments. The clearing house is managed by the RBI, State Bank of India or any other Bank nominated by RBI. In case a bank has many branches within the area of a clearing house, it nominates one branch to act as the 'nodal' branch of that Bank for all the branches within that area. This nodal branch collects instruments to be presented to other branches also. The accounts of all member banks are maintained by the clearing house. All member banks have to pay an agreed sum to the bank managing the clearing house for meeting the cost of infrastructure and services it provides to them.

2.6 In addition to the regular clearing houses as discussed above, Electronic Clearing Services (ECS) is also in vogue. ECS takes two forms: ECS credit or ECS debit.

- In the case of ECS credit, there is a single receiver of funds from a large number of customers, e.g., public utilities, mutual funds, etc. The beneficiary (i.e., the receiver of funds) obtains mandate from its customers to withdraw funds from their specified Bank accounts on a particular date. These customers may have accounts with different banks in the same clearing house area. Before the specified date, the beneficiary compiles Bank-branch-wise particulars of the accounts to be debited and furnishes the details in the electronic media like a floppy disc to its own Bank which, in turn, arranges to provide them to the banks concerned, through the clearing house, for verification of particulars of accounts. Any discrepancies are rectified and, on the specified date, the accounts are debited by the respective banks and the beneficiary gets the credit.
- In the case of ECS debit, there is a single account to be debited against which a number of accounts with a number of banks in the same clearing house area are credited. This system is useful for distribution of dividend/ interest, payment of salaries by large units, etc.

2.7 Role-out of Speed Clearing is one of the many initiative taken by RBI for improving efficiency in the time frame and process of collection of cheques.

Cheque Truncation System (CTS) was pioneered by Reserve Bank of India for faster clearing of cheques. It is implemented since 1st august 2013.It involves sending an electronic image of the cheque together with Magnetic Ink Character Recognition (MICR) Data and other relevant fields like date of presentation, presenting bank names etc. This procedure eliminates the need for physical transfer of cheques across branches, except in certain cases.CTS ensures faster clearing, lesser chances of fraud with no fear of loss of cheque in transit.

Receipt of Foreign Contribution on behalf of the Registered Persons/Organization

2.8 Scheduled Banks also handle the foreign contribution receipt on behalf of the registered persons/ organization as per the Foreign Contribution (Regulation) Act, 2010. Banks need to ensure that the concerned persons/ organization are registered with the Central Government or has obtained the prior permission to receive such foreign contribution if required by law, and that no branch other than the specified branch accepts ‘foreign contribution’.

Cash Management Product

2.9 It is a derivative of the collection business; this facility is provided for expeditious transfer of funds collected by a customer at the specified centre in the country to his central account with the use of computers/ satellites. It is particularly useful for large units which have their sales/ collection network in a very wide geographical area. Only selected branches of a bank may handle the business due to the infrastructural requirements.

Issuance of Letters of Credit and Guarantees

2.10 These are two important services rendered by banks to customers engaged in business, industrial and commercial activities. A letter of credit (LC) is an undertaking by a bank to the payee (the supplier of goods and/or services) to pay to him, on behalf of the applicant (the buyer) any amount up to the limit specified in the LC, provided the terms and conditions mentioned in the LC are complied with. The guarantees are required by the customers of banks for submission to the buyers of their goods/services to guarantee the performance of contractual obligations undertaken by them or satisfactory performance of goods supplied by them, or for submission to certain departments, like, excise and customs, electricity boards, or to suppliers of goods, etc. in lieu of the stipulated security deposit.

Merchant Banking Business

2.11 Many bank branches act as collection agents to issue business for merchant bankers. The customer and the bank have to agree to the modalities of the scheme, like names of branches authorized as collecting branches, the procedure for retaining the subscription and its remittance periodically, the documents required by the customer from the collecting branches, etc.

Credit Cards

2.12 The processing of applications for issuance of credit cards is usually entrusted to a separate division at the central office of a bank. The dues against credit cards are collected by specified branches. Many of them also act as 'cash points' to provide cash to the cardholder on demand up to the specified limits. Most credit cards issued by banks are linked to one of the international credit card networks, like, VISA, Master, or Amex.

Technology-based Services

2.13 Some banks have started providing internet banking services and phone banking services. Some banks, acting as stock brokers, also provide facility to their customers to buy or sell securities on stock exchanges through the internet. The fast changing technology has synchronized banking facility in such a way that the customer need not physically attend for any transactions. The banks are now providing the facility of payment of utility bills, railway reservation, and tax deposition through ATM/internet banking and are also providing value added services like recharge facility to mobile phone users.

Dividend/ Interest/ Refund Warrants

2.14 Many entities require facilities for distribution of funds to their shareholders and others. For this purpose, they issue warrants in favour of shareholders/others payable at designated branches of specified banks, with a prior arrangement with the banks concerned. The aggregate amount of the warrants or other instruments issued is deposited by the entity with a nodal branch. The designated branches pay the warrants at par when presented to them.

Safe-keeping Services

2.15 Banks provide services for safe keeping of the scrips and valuables of customers in their vaults. A receipt is issued to the customer by the branch at the time of deposit of the items and an acknowledgement is obtained from him at the time of delivery. Each transaction - a receipt or delivery - is duly recorded in appropriate register(s) and periodically, the items physically available are cross checked with the balances as per registers.

Lockers

2.16 This facility is provided to customers for protecting their valuables, in lockers. The branch has no knowledge of the contents of the locker. Only the account holder (the hirer) or his representative, duly authorized by the account holder, can operate on the locker. Each access to the locker is properly recorded in the appropriate registers.

Handling Government Business

2.17 Banks act as agents of RBI for receipts and payments on behalf of various government departments like income tax, central excise, sales tax, etc. There are authorized branches to handle the specified type of work. Normally, a specified branch acts as a nodal branch for a particular segment of the government business within a given geographical area. The responsibility of the nodal branch includes obtaining details of transactions from the linked branches and to reconcile their accounts *inter se* and with the department concerned. Banks are remunerated for handling this business by way of service charges which are usually as agreed or a stated percentage of the collections or payments, as the case may be.

Depository Participant (DP) Services

2.18 The depository system is meant to facilitate quick transfer of stock market securities in a dematerialized form from the seller to the buyer by using satellite connectivity. The depository scheme is operated presently by two depositories - Central Depository Services Limited and National Securities Depository Limited. Depository participants, i.e., bank branches providing depository services are in effect agents of the depository concerned. Each participating branch has to get itself registered with a depository. The customer has to open an account with the branch which provides the DP services. This account is debited by the branch with the securities sold by the account holder and credited with the purchases.

Automated Teller Machine (ATMs)

2.19 Operations on ATMs are through a card (popularly known as ATM card) which contains information about the cardholder in a magnetic form. The cardholder has to also use the password (also known as Personal Identification Number, i.e., PIN) to carry out any transaction through ATM. Earlier, ATMs were used merely as cash dispensing machines but now-a-days, other services like, issue of drafts, deposit of cash and instruments, balance enquiry, etc., are also being provided by many banks. ATMs may be on-site (i.e., housed in the branch premises) or off-site. The transactions routed by the customers through the ATMs may be entered into the books of account of the branch either on-line (i.e., simultaneously with the transactions) or off-line. However, on an off-line mode, the proper recording of transactions needs to be ensured.

Exchange of Notes

2.20 Banks exchange mutilated notes from the public for good quality notes. These mutilated notes are periodically sent to the RBI which gives equivalent credit to the branch concerned.

Debit Cards

2.21 Debit cards are issued by the bank where customer is having his /her account. The debit cards are generally issued from central office of the bank. The Debit Card facilitates the customer to pay at any authorized outlet as well as to withdraw money from ATM from his account. The debit cards are sometimes networked with inter-bank network.

Auto Sweep Facility in Saving Account

2.22 The banks are offering auto sweep facility in saving accounts of their customers where balance exceeding a certain limit automatically gets transferred to term deposit account having higher rate of interest and in case of need, the funds in term deposit automatically get transferred to saving account.

Third Party Advertisement on ATM Network

2.23 The banks are providing advertisement facility to the vendors on ATM Network. The advertisement on ATM Network provides the opportunity of earning revenue to the Bank.

Derivatives

2.24 Financial derivatives are gaining importance in India. Banks are offering derivative options against exchange fluctuation losses.

Reverse Mortgage

2.25 Reverse mortgages are powerful tools that help eligible homeowners obtain a tax-free cash flow. Over two hundred thousand people have already used Reverse mortgages to enhance their income after retirement. A reverse mortgage is a government sponsored and insured loan that requires no payments during the period of time, borrowers live in their home. Reverse mortgages enable eligible homeowners to access the money they have built up as equity in their homes. Conceptually, a reverse mortgage seeks to monetize the house as an asset and specifically the owner's equity in the house.

Prepaid Payment Instruments in India

2.26 Pre-paid payment instruments are payment instruments that facilitate purchase of goods and services against the value stored on such instruments. The value stored on such instruments represents the value paid for by the holders by cash, by debit to a bank account, or by credit card. The pre-paid instruments can be issued as smart cards, magnetic stripe cards, internet accounts, internet wallets, mobile accounts, mobile wallets, paper vouchers and any such instrument which can be used to access the pre-paid amount (collectively called Prepaid Payment Instruments (PPI). The pre-paid payment instruments that can be issued in the country are classified under three categories viz. (i) Closed system PPI (ii) Semi-closed system PPI and (iii) Open system PPI. In the process of moving from cash based payments to electronic payments to achieve the vision of less- cash society, a new category of semi-closed prepaid payment instrument is being introduced with certain features which is named as PPI for mass transit system (PPI-MTS) vide RBI latest master circular DPSS. CO.PD No. 2/02 14-006/2015-2016 dated 01.07.2015 on issuance and operation of prepaid instrument in India.

"Issuer" may be the persons operating the payment systems issuing prepaid payment instruments to individuals/organizations. The money so collected is used by these persons to make payment to the merchants who are part of the acceptance arrangement directly, or through a settlement arrangement. Further, it requires that other non-bank persons issuing PPI are need to maintain their outstanding balance in an escrow account with any scheduled commercial bank subject to the following conditions:

- The amount so maintained be used only for making payments to the participating merchant establishments.
- No interest is payable by the bank on such balances.
- A quarterly certificate from the auditors be submitted certifying that the entity has been maintaining adequate balance in the account to cover the outstanding volume of payment instruments issued.

- The entity shall also submit an annual certificate, as above, coinciding with the accounting year of the entity to the Reserve Bank of India.
- Adequate records indicating the daily position of the value of instruments outstanding vis-à-vis balances maintained with the banks in the escrow accounts be made available for scrutiny to the Reserve Bank or the bank where the account is maintained on demand.

Further, RBI vide its Master Circular No. DPSS.CO.PD.PPI.No. 2/02.14.006/ 2015-2016 dated July 1, 2015 on "Issuance and operation of Prepaid Payment Instruments in India – Auditor Certificate on the balances in Escrow account" requires a quarterly certificate on the balances held in the Escrow account in accordance with the above Guidelines, from an auditor within a fortnight from the end of the quarter to which it pertains.

Para-banking Activities

2.27 Banks also undertake certain eligible financial services or para-banking activities either departmentally or by setting up subsidiaries. However, banks can set up subsidiary for undertaking such activities only with prior approval of RBI. Some of those activities are given below:

- *Equipment Leasing, Hire Purchase and Factoring Services*: Banks also undertake equipment leasing, hire purchase and factoring services as departmental activities.
- *Mutual fund business*: Banks are not permitted to directly undertake mutual fund business but sponsor mutual funds, subject to the RBI guidelines in this regard. Banks normally refer clients to these mutual funds and earn a commission in return. Banks may enter into agreement with mutual funds for marketing, the mutual fund units subject to the terms and conditions specified in the RBI master circular on "Para Banking Activities"
- *Money Market Mutual Funds (MMMFs):* Banks can also sponsor MMMFs business subject to the prior approval of the RBI. The MMMFs are, however, subject to regulation by the Securities and Exchange Board of India. Banks also, at time, provide cheque writing facilities for MMMFs subject to the RBI guidelines in this regard.

- *Entry of banks into Insurance Business*:

  Banks intending to set up insurance joint ventures with equity contribution on risk participation basis or making investments in the insurance companies for providing infrastructure and services support should obtain prior approval of Reserve Bank of India before engaging in such business. However, insurance business will not be permitted to be undertaken departmentally by the banks.

- *Primary Dealership Business* : Banks can undertake primary dealership business (PD Service) subject to the approval of the RBI and after satisfying certain eligibility criteria prescribed by the RBI:

  (A) Banks, which do not at present, have a partly or wholly owned subsidiary and fulfill the following criteria:

    a. Minimum Net Owned Funds of Rs. 1,000 crore.

    b. Minimum CRAR of 9%.

    c. Net NPAs of less than 3% and a profit making record for the last three years.

  (B) Indian banks which are undertaking PD business through a partly or wholly owned subsidiary and wish to undertake PD business departmentally by merging/taking over PD business from their partly/wholly owned subsidiary subject to fulfilling the criteria mentioned in A (a) to (c) above.

  (C) Foreign banks operating in India who wish to undertake PD business departmentally by merging the PD business being undertaken by group companies subject to fulfillment of criteria at A (a) to (c).

- *Pension Funds Management* :Banks have been permitted to undertake Pension Funds Management (PFM) through their subsidiaries set up for the purpose subject to their satisfying the eligibility criteria prescribed by Pension Fund Regulatory and Development Authority (PFRDA) for Pension Fund Managers. PFM cannot be undertaken departmentally. Banks intending to undertake pension funds management should follow the guidelines set out in the RBI Master Circular No.DBR.No.

FSD.BC.19/24.01.001/2015-16 dated July 1, 2015 on "Para - Banking Activities".

- *Portfolio Management Services*: The general powers vested in banks to operate Portfolio Management Services and similar schemes have been withdrawn vide RBI circular DBOD.No.BC.73/27.07.001/94-95 dated June 7, 1994 on Acceptance of Deposits/Funds under Portfolio Management Scheme. No bank therefore is permitted to, restart or introduce any new PMS or similar scheme in future without obtaining specific prior approval of the RBI. However, bank-sponsored NBFCs are allowed to offer discretionary PMS to their clients, on a case-to-case basis. The banks operating PMS or similar scheme with specific prior approval of RBI have to strictly observe the conditions given in RBI Master Circular No. DBR.No.FSD.BC.19/24.01.001/2015-16 dated July 1, 2015 on "Para Banking Activities".
- *ReferralServices*: Banks can offer referral services to their customers for financial products subject to the following conditions:
  - (a) The bank/third party issuers of the financial products should strictly adhere to the KYC/AML guidelines in respect of the customers who are being referred to the third party issuers of the products.
  - (b) The bank should ensure that the selection of third party issuers of the financial products is done in such a manner so as to take care of the reputational risks to which the bank may be exposed in dealing with the third party issuers of the products.
  - (c) The bank should make it explicitly clear upfront to the customer that it is purely a referral service and strictly on a non-risk participation basis.
  - (d) The third party issuers should adhere to the relevant regulatory guidelines applicable to them.
  - (e) While offering referral services, the bank should strictly adhere to the relevant RBI guidelines.
- *Underwriting of Corporate Shares and Debentures*: Banks can undertake underwriting of corporate shares and debentures within the ceiling prescribed for the bank's exposure to capital markets and subject to the

provisions contained in the Section 19(2) and 19(3) of the Banking Regulation Act, 1949. The guidelines contained in the SEBI (Underwriters) Rules and Regulations, 1993 and those issued from time to time are also to be complied with. Moreover, banks should not underwrite issue of Commercial Paper by any Company or Primary Dealer and not extend Revolving Underwriting Facility to short term Floating Rate Notes/Bonds or debentures issued by corporate entities. However, with effect from April 16, 2008, banks may exclude their own underwriting commitments, as also the underwriting commitments of their subsidiaries, through the book running process for the purpose of arriving at the capital market exposure both on a solo and consolidated basis.

- *Underwriting of Bonds of Public Sector Undertakings*: Banks can play a useful role in relation to issue of bonds by Public Sector Undertakings (PSUs) by underwriting a part of these issues. They may also subscribe outright initially but sell them later to the public with the aid of their wide branch network. It should, however, be ensured that the increase in the holdings of public sector bonds by banks arising out of their underwriting or subscription is kept within reasonable limits. While undertaking the underwriting of bonds of PSUs, banks should formulate their own internal guidelines as approved by their Boards of Directors on investments in and underwriting of PSU bonds, including norms to ensure that excessive investment in any single PSU is avoided and that due attention is given to the maturity structure of such investments.
- *Retailing of Government Securities*: Banks are permitted to undertake the business of retailing of Government securities with non-bank clients subject to the following conditions:

  (a) Banks are free to buy and sell Government Securities on an outright basis at prevailing market prices without any restriction on the period between sale and purchase.

  (b) Banks shall not undertake ready forward transactions in Government Securities with non-bank clients.

(c) The retailing of Government Securities should be on the basis of ongoing market rates / yields emerging out of secondary market transactions.

(d) No sale of Government Securities should be effected by banks unless they hold the securities in their portfolio either in the form of physical scraps or in the SGL Account maintained with the Reserve Bank of India.

(e) Immediately on sale, the corresponding amount should be deducted by the bank from its investment account and also from its SLR assets. f) Banks should put in place adequate internal control checks/ mechanism in this regard.

(g) These transactions should be subjected to concurrent audit as per RBI's extant instructions and should also be looked into by the auditors at the time of bank's statutory audit.

- *Sponsors to Infrastructure Debt Funds (IDFs)* : In order to accelerate and enhance the flow of long term funds to infrastructure projects for undertaking the Government's ambitious programme of infrastructure development, scheduled commercial banks have been allowed to act as sponsors to Infrastructure Debt Funds (IDFs). IDFs can be set up either as Mutual Funds (MFs) or as Non-Banking Finance Companies (NBFCs). While IDF-MFs are regulated by SEBI, IDF-NBFCs are regulated by Reserve Bank of India (RBI). Banks can sponsor IDF-MFs and IDF-NBFCs with prior approval from RBI subject to the conditions given in the RBI Master Circular No. DBR.No.FSD.BC.19/24.01.001/2015-16 dated July 1, 2015on "Para - Banking Activities".
- *Membership of currency derivative segment of SEBI approved Stock Exchanges*: Scheduled commercial banks (AD Category I) have been permitted to become trading / clearing members of the currency derivatives segment to be set up by the Stock Exchanges recognized by SEBI, subject to their fulfilling the following prudential requirements:

  (a) Minimum net worth of ₹ 500 crores,

(b) Minimum CRAR of 10%

(c) Net NPA not exceeding 3%

(d) Net Profit for last 3 years

Banks which fulfill the conditions mentioned above should lay down detailed guidelines with Board's approval for conduct of this activity and management of risks. It should be ensured that the bank's position is kept distinct from the clients' position. In case of supervisory discomfort with the functioning of a bank, the Reserve Bank may impose restrictions on the bank regarding the conduct of this business as it deems fit. The banks which do not meet the above minimum prudential requirements are permitted to participate in the currency futures market only as clients.

Note: The RBI has issued a Master Circular No.DBR.No.FSD.BC.19/24.01.001/2015-16dated July 1, 2015on "Para-Banking Activities" containing instructions/guidelines issued by it to banks in respect of their para banking activities.

Chapter 3
Organizational and Operational Structure of Banks

3.1 While the exact organizational structure may differ from one bank to another, most large-sized banks have a four-tier structure - head office, zonal offices, regional offices and branches (the nomenclature may, however, vary among banks), each tier of the structure being responsible for performing the functions specified by the Head Office. However, there are some banks having three tier structures without zonal office concept.

3.2 At the apex level, there is the head office of the Bank whose main functions are as follows:

- Laying down policies and procedures for smooth and efficient functioning of the Bank and to review them periodically.
- Deciding on the extent of powers-financial and administrative–which may be vested in various functionaries of the Bank.
- Planning and performance budgeting.
- Asset-liability management.
- Laying down lending policy of the Bank, the risk management guidelines, and the rehabilitation and recovery guidelines including policies for compromise, settlement and write-off.
- Deciding about the interest rates on both the deposits and the loans as well as about charges for various services and review interest rates and charges periodically.
- Treasury and investment management (usually handled by the head office, though in some cases, select large branches may also be involved in this function).
- Monitoring and controlling the functioning of various offices of the Bank. Periodic inspections and internal audit are important constituents of such monitoring and control mechanism.

- Reconciling the transactions among various offices of the Bank.
- Introducing new products and services and reviewing the existing ones.
- Issuing instructions to branches and other offices from time to time on matters deserving their attention or requiring compliance by them.
- Publish the credit policy after surveying the economic scenario of the country.
- Submission of various information to RBI and Ministry of Finance, Government of India.
- HR development function and framing of policy of development of personnel to utilize their talent.
- To obtain various licenses for opening new branches and other financial function as per statutory rule.
- To publish balance sheet and profit and loss statement of the Bank and organize annual general meeting of the shareholders.
- To keep close track with the technology building and take suitable up-gradation.
- Technology Management including management of CBS and disaster management.

3.3 At tier II, there are the zonal offices which are responsible for overall workings of the branches in their areas of operation. Zonal offices act as a link between the branches and the head office, either directly or through regional offices.

3.4 Below the zonal offices, there are the regional offices which are the immediate controllers of the branches under their jurisdiction. They are responsible for business development, compliance with the laid down systems and procedures, satisfactory customer service, quick redressal of complaints and submissions of the required statements/reports/returns by branches under their jurisdiction. They are also responsible for smooth functioning of the branches under them. Regional office organize monthly review meeting in order to judge the performance of the branch under their control in all area of operation and discuss on the internal audit and inspection report of the branch and the report of the auditor of the branch.

3.5 Branches are lowest in the hierarchy of the banking organization structure. In fact, the banking operations (i.e., accepting deposits and making loans) actually take place at the branch level. Their jobs are numerous, practically everything in relation to banking, except for pricing of products/services and the policy formulation

Branch Network of Commercial Banks

3.6 Apart from the term-lending institutions, commercial banks are arguably the most important constituent of the banking system in India. To carry out their functions effectively, these banks have established a large network of branches in India. Based on their location, these 'domestic' branches are commonly classified into rural branches, semi-urban branches, urban branches and metro branches. Apart from these domestic branches, some banks have also established offices abroad. The foreign offices of banks are generally of the following types:

- *Full-fledged branches* - Such branches transact all kinds of banking business.
- *Off-shore banking units* - Such branches transact foreign exchange business of any kind except domestic banking business with the residents/ corporations, etc., domiciled in the country concerned.
- *Subsidiaries* - The laws in some countries do not permit foreign banks to open their branches in those countries. Therefore, Indian banks have to set up wholly or partly owned subsidiaries in such countries. Further for operational regions, commercial bank may prefer to operate through subsidiaries, if permitted, instead of opening branches.
- *Representative offices* - Such branches do not transact any banking business. The objective behind setting up such offices is to maintain close liaison with the important bodies there to promote mutual business interests.

3.7 Generally, branches conduct a variety of banking business under one roof. Recently, however, the trend of creating 'thrust based' or 'focus-based' branches is on the rise. This has led to setting up of branches by banks exclusively for a specified segment of their clients. Presently, such specialized branches are generally of the following types (nomenclature may, however, vary from bank to bank):

- Personal Banking branches, catering to the needs of individual customers only.
- Commercial or Industrial Finance branches, catering to the needs of industries in the small, medium and/or large sectors.
- Recovery branches, which deal only with the recovery aspects of non-performing advances which were originally granted at other branches of the Bank.
- Housing Finance branches which deal only with housing loan proposals - from individuals, and in some cases, also from the developers of housing units.
- Agricultural Finance branches, catering to the needs of the agriculture sector only.
- Service branches, handling only the local clearing instruments received from outstation branches or from other local branches of the Bank for collection.
- Commodity specific branches, which handle the accounts, predominantly borrowable accounts, of the units belonging to a particular industry, e.g., leather, diamonds.
- Overseas or International Banking or Foreign Exchange branches catering to the banking needs of those enterprises which are engaged in imports into/exports from India.
- Corporate banking/SME/SSI branches, catering exclusively to the requirements of the large, medium and small scale industrial units.
- NRI (Non-Resident Indian) branches, catering exclusively to the banking needs of NRIs.
- Securities branches, dealing only with the securities portfolio of the Bank.

3.8 The trend towards specialization may, in future, cause the opening of dedicated branches of various other segments of clients such as, government business, remittance business, trade sector business, lockers business, rehabilitation, education loans, etc.

Role of the Reserve Bank of India as the Central Bank

3.9 The RBI is the central bank of our country. As such, RBI is responsible for development and supervision of the constituents of the Indian financial system, which comprises banks and non-banking financial institutions.~~,~~ RBI also determines, in conjunction with, the Central Government, the monetary and credit policies keeping in mind the need of the hour. Its important functions are:

- issuance of currency and regulation of currency issue;
- acting as banker to the central and state governments;
- acting as banker to commercial and other types of banks including term-lending institutions;
- Besides, RBI has also been entrusted with the responsibility of regulating the activities of commercial and other banks. No bank can commence the business of banking or open new branches without obtaining licence from RBI;
- The RBI also has the power to inspect any bank. The Banking Regulation Act, 1949 provides the legal framework for regulation and supervision of banks. This statute, together with some provisions in the Reserve Bank of India Act, 1934, State Bank of India Act, 1955, State Bank of India (Subsidiary Banks) Act, 1959 and Banking Companies (Acquisition and Transfer of Undertakings) Acts, 1970 & 1980, empowers the Reserve Bank of India (RBI) to prescribe standards; and
- monitor liquidity, solvency and soundness of banks, so as to ensure that depositors' interests are protected at all times.

3.10 Periodical inspections of banks under section 35 of the Banking Regulation Act, 1949 are undertaken as a follow-up of the bank licensing regulation and objectives as laid down in section 22 of the Banking Regulation Act, 1949. The substantive objective of the statutory inspections has been to verify whether the conditions subject to which the bank has been issued licence to undertake banking business in terms of sub-section (3) of section 22 [including sub-section (3A) for foreign banks] continue to be fulfilled by it. The conditions include:

(a) the bank "is or will be in a position to pay its present or future depositors in full as their claims accrue" (i.e., it is solvent and has adequate liquidity);

(b) the bank "has adequate capital structure and earning prospects";

(c) "the affairs of the (banking) company are not being, or are not likely to be, conducted in a manner detrimental to the interests of its present or future depositors"; and

(d) "the general character of the management of the bank is not prejudicial to the public interest or the interest of its depositors" (i.e., it has sound operational systems and adequate controls operated by a prudent management).

Section 22(4) of the Banking Regulation Act, 1949 authorises the RBI to cancel the banking licence "if at any time, any of the conditions referred to in sub-section (3) and sub-section (3A) is not fulfilled".

3.11 Based on the recommendations of a High Level Steering Committee (HLSC) for Review of Supervisory Processes of Commercial Banks, the Reserve Bank of India had in September 2012, introduced a Supervisory Program for Assessment of Risk and Capital (SPARC) for commercial banks. This Risk Based Supervision (RBS) approach, helps the regulator in focusing on evaluating both present and future risks, identifying incipient issues and facilitating prompt intervention/ early corrective action - as against the earlier compliance-based and transaction testing approach (CAMELS) which was more in the nature of a 'point in time' assessment. The RBS approach also benefits the regulator by optimizing its use of supervisory resources and assisting the regulated entities in improving their risk management systems, oversight and controls.

3.12 RBI is empowered under section 21 of the Banking Regulation Act, 1949, to control advances by banks, in general, or by any bank in particular. Among the measures that the RBI can adopt for this purpose are to prescribe purposes and extent of advances, margin requirements, maximum exposure to a single borrower, rate of interest and other terms and conditions, etc. Besides these measures (which are usually called 'selective credit control' measures), RBI also controls the total volume of bank credit by varying bank rate through open market operations or by varying cash reserve and similar requirements.

3.13 Bank rate refers to the rate of interest at which the RBI re-discounts the first class bills of exchange or other eligible instruments from banks. Variations in bank rate affect the interest rates charged by banks – generally, interest rates of banks move up or down in tandem with movements in bank rate.

3.14 Under Base Rate system which came into effect from July 1, 2010, all categories of domestic rupee loans of banks are priced only with reference to the Base Rate, subject to certain conditions. For monetary transmission to occur, lending rates have to be sensitive to the policy rate. At present, banks follow different methodologies for computing their Base Rate like, average cost of funds method, marginal cost of funds, blended cost of funds (liabilities), etc.

3.15 Open market operations involve sale or purchase of government securities in the open market. When RBI buys government securities from banks in the open market, the funds in the hands of selling banks increase, enabling them to expand credit, and vice versa.

3.16 Banks are required to maintain at least a prescribed minimum percentage of their demand and time liabilities in India in the form of cash and/or current account balances with the RBI (called 'cash reserve ratio'). Additionally, they are required to maintain a further percentage in the form of cash and/or other liquid assets (called 'statutory liquidity ratio'). Varying the cash reserve ratio and/or statutory liquidity ratio enables the RBI to increase or decrease (as the case may be) the funds available to banks for lending and other similar purposes.

3.17 A major development that has implications for banks throughout the world is the "International Convergence of Capital Measurement and Capital Standards", generally, known as the Basel Accord. While the implementation of Basel 2 is expected to lead to improved risk management systems in banks, promote a more robust supervisory framework and strengthen market discipline, with the cumulative effect being greater financial stability, Basel 3 ensures better quality of capital and robust liquidity risk management. In view of its impending implementation, RBI is in a continuous dialogue with the banks regarding their preparedness to introduce the necessary up-gradation in their internal systems, data collection machinery, quality of MIS, training facilities and availability of improved skill sets.

3.18 The smooth functioning of the payment and settlement systems is a prerequisite for stability of the financial system. In order to have focused attention on payment and settlement systems, a Board for Regulation and Supervision of Payment Systems (BPSS) was set up in March, 2005. The launch of the Real

Time Gross Settlement System (RTGS) and NEFT (National Electronic Funds Transfer) has led to a reduction of settlement risk in large-value payments in the country. Similarly, IMPS (Interbank Mobile Payment Service/Immediate Payment Service) is a mobile based payment mechanism introduced by the National Payments Corporation of India to allow customers to transfer money instantly, facilitating instant remittance across multiple platforms. The setting up of NSDL and CDSL for the capital market settlements and CCIL for G-sec, forex and money market settlements have improved efficiency in market transactions and settlement processes. A series of legal reforms to enhance the stability of the payment systems have been carried out. With the introduction of the Payments and Settlement Act in 2008, the Reserve Bank has the legislative authority to regulate and supervise payment and settlement systems in the country.

3.19 In India, deposit insurance is provided by the Deposit Insurance and Credit Guarantee Corporation (DICGC), a wholly owned subsidiary of the Reserve Bank of India. Deposit insurance in India is mandatory for all banks (commercial/co-operative/RRBs/LABs). It covers all kinds of deposits except those of foreign governments, Central/State Governments, inter-bank, deposits received abroad and those specifically exempted by DICGC with prior approval of the Reserve Bank. The premium charged for deposit insurance is on a flat rate basis, which is currently 10 paise per ₹100 of assessable deposits with a statutory ceiling on premium at 15 paise. The premia to be paid by the insured banks are computed on the basis of their assessable deposits. Insured banks pay advance insurance premia to the Corporation semi-annually within two months from the beginning of each financial half year, based on their deposits as at the end of previous half year. The amount of coverage is presently limited to ₹1 lakh per depositor and extends to deposits held in the same right and in the same capacity.

3.20 Banks and financial institutions (FIs) have also been advised by RBI to follow certain customer identification procedure for opening of accounts and monitor transactions of suspicious nature for the purpose of reporting the same to appropriate authority. These 'Know Your Customer' (KYC) guidelines have been revisited in the context of the recommendations made by the Financial Action Task Force (FATF) on Anti Money Laundering (AML) standards and on Combating Financing of Terrorism (CFT). Detailed guidelines based on the recommendations of FATF and the paper issued on Customer Due Diligence (CDD) for banks by the Basel Committee on Banking Supervision (BCBS), with suggestions wherever considered necessary, have been issued. Banks/FIs have been advised by RBI to ensure that a proper policy framework on 'Know Your Customer' and Anti-Money Laundering measures is formulated and put in place with the approval of their Boards. The objective of KYC/AML/CFT guidelines is to prevent banks/FIs from being used, intentionally or unintentionally, by criminal elements for money laundering or terrorist financing activities. KYC procedures also enable banks/FIs to know/understand their customers and their financial dealings better and manage their risks prudently. Foreign Account Tax Compliance Act (FATCA) is a US law, which was enacted in March 2010 by US Government which was aimed at preventing tax evasion through offshore assets by US citizens and US residents. Foreign Financial Institutions (FFIs) such as the Bank that enter into a FATCA FFI agreement with the US government are required to conduct certain due-diligence to identify its US clients (individual and entity) and report on their accounts to the US Internal Revenue Service (IRS).

3.21 India has signed the Inter-Governmental Agreement (IGA) with USA for improving international tax compliance and implementing the Foreign Account Tax Compliance Act (FATCA). India has also signed a multilateral agreement on June 3, 2015, to automatically exchange information based on Article 6 of the Convention on Mutual Administrative Assistance in Tax Matters under the Common Reporting Standard (CRS), formally referred to as the Standard for Automatic Exchange of Financial Account Information (AEoI).

3.22 Apart from directions relating to operational matters, RBI also issues, from time to time, guidelines on accounting matters to be followed by banks. These guidelines have a profound effect on annual accounts of banks. The text of the notifications/circulars/guidelines, etc., issued by the RBI are normally also available on its website www.rbi.org.in.

Chapter 4
Legal and Regulatory Framework of Banks

Enactments Governing the Functioning of Banks

4.1 There is an elaborate legal framework governing the functioning of banks in India. The principal enactments which govern the functioning of various types of banks are:

- Banking Regulation Act, 1949
- Banking Companies (Nationalization of Undertakings) Act, 1970
- Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970
- Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980
- Negotiable Instruments Act, 1881
- State Bank of India Act, 1955
- State Bank of India (Subsidiary Banks) Act, 1959
- Regional Rural Banks Act, 1976
- Companies Act, 2013
- Co-operative Societies Act, 1912 (or the relevant State Cooperative Act)
- Information Technology Act, 2000
- Prevention of Money Laundering Act, 2002
- Credit Information Companies (Regulation) Act, 2005
- Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
- Recovery of debts due to Banks and Financial Institutions Act, 1993
- Transfer of Property Act, 1882

- Indian Stamp Act, 1899
- Power of Attorney Act ,1882
- The Insolvency and Bankruptcy Code, 2016
- Foreign Exchange Management Act, 1999
- Uniform Customs and Practice for Documentary Credits (UCP 600)
- Payment and Settlement Systems Act, 2007

4.2 Besides, the above enactments, the provisions of the Reserve Bank of India Act, 1934, also affect the functioning of banks. The Act gives wide powers to the RBI to give directions to banks; such directions also have considerable effect on the functioning of banks.

Salient Provisions of Banking Regulation Act, 1949

4.3 Of the above, the Banking Regulation Act, 1949 is the most important as it affects the functioning of all institutions carrying on banking business. Other enactments relate only to certain specific type(s) of banks. Some of the important provisions of the Act are briefly described below since familiarity with them is essential for the performance of the duties of an auditor. It needs to be emphasized that the ensuing discussion is not an exhaustive discussion on all the relevant provisions of the Act.

Definition of Banking Companies

4.4 A *banking company* means "any company which transacts the business of banking in India" [section 5(c) of the Banking Regulation Act]. The term 'company' for this purpose covers companies registered in India as well as foreign companies, i.e., companies incorporated outside India and having a place of business within India [section 5(d)].

Forms of Business of Banking Companies

4.5 'Banking' is defined as "the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise" [section 5(b)]. It has been clarified that any company which is engaged in the manufacture of goods or carries on any trade and which accepts deposits of money from the public merely for the purpose of financing its business as such manufacturer or trader, shall not be deemed to transact the business of banking *[Explanation* to section 5(c)].

4.6 Section 6 of the Act permits a banking company to engage in certain forms of business in addition to the business of banking. Besides the forms of business specifically listed in clauses (a) of sub-section (1) of section 6, a banking company may do "all such other things as are incidental or conducive to the promotion or advancement of the business of the company" [clause (n) of sub-section(1) of section 6]. Under clause (o), a banking company may engage in any other form of business (besides those covered by other clauses) which the Central Government may, by Notification in the Official Gazette, specify as a form of business in which it is lawful for a banking company to engage.

4.7 Under sub-section (2) of section 6, a banking company is prohibited from entering into any form of business other than those covered by subsection (1) of the said section. Section 8specifically prohibits a banking company from buying, selling or bartering of goods except in connection with the realization of a security held by it. It also prohibits a banking company from engaging in any trade or buying, selling or bartering of goods for others except in connection with collecting or negotiating bills of exchange or in connection with undertaking the administration of estates as executor, trustee or otherwise. However, the above prohibitions are not applicable to any business specified by the Central Government in pursuance of clause (o) of sub-section (1)of section 6.

Licensing of Banking Companies

4.8 Section 22 of the Act prohibits a company from carrying on banking business in India unless it holds a license issued by the RBI. The license may be a conditional license. The license may be cancelled if the company ceases to carry on banking business in India or fails to comply with the conditions of the license or fails to fulfil any other condition laid down in the section.

Power to Suspend Operation of the Act

4.9 On a representation made by the RBI in this behalf, the Central Government may suspend the operation of the Act or of any provision thereof for a period up to 60 days either generally orin relation to any specified banking company. In case of a special emergency, the Governor of the RBI or, in his absence, any authorized Deputy Governor may also similarly suspend such operation for a period up to 30 days. In either case, the Central Government may extend the period of suspension from time to time for periods not exceeding 60 days at any one time. The total period of suspension cannot, however, exceed one year [section4].

Requirements as to Minimum Paid-up Capital and Reserves and Regulation of Capital

4.10 Section 11 of the Act lays down the requirements as to minimum paid-up capital and reserves. Different limits have been laid down for banking companies incorporated outside India and other banking companies. Under section 12, the capital of a banking company can consist of ordinary (i.e., equity) shares only, except where preference shares have been issued prior to July 1,1944 or where the banking company has been incorporated before January 15, 1937.

Restrictions on Opening and Transfer of Places of Business

4.11 Under Section 23, prior permission of the RBI is required for opening of new, or transfer of existing, places of business in India. Similar permission is required by a banking company incorporated in India for opening a new, or transferring an existing, place of business outside India. The above restrictions, however, do not cover the change of location of an existing place of business within the same city, town or village. Opening of a temporary place of business for a period not exceeding one month is also exempted provided the conditions laid down in this behalf are satisfied. The term 'place of business' includes any sub office, pay office, sub-pay office and any place of business at which deposits are received, cheques are encashed or monies are lent.

4.12 It may be noted that recently, the RBI has permitted banks to open new places of business or transfer existing ones without obtaining specific permission from it provided certain conditions specified by the RBI in this behalf are satisfied.

Inspection by the RBI

4.13 Wide powers have been given to the RBI under section 35for inspection of any banking company and its books and accounts. The Central Government can also direct the RBI to cause such an inspection.

Power of the RBI to Give Directions

4.14 The RBI is empowered to issue such directions to banking companies generally or to any banking company in particular as it deems fit in public interest, or in the interest of banking policy, or to prevent the affairs of any banking company from being conducted in a manner detrimental to the interests of the depositors or in a manner prejudicial to the interests of the banking company, or to secure the proper management of any banking company generally (section 35A). The RBI is also empowered to caution or prohibit banking companies generally or any particular banking company against entering into any particular transaction or class of transactions, and generally give advice to any banking company [Clause (a) of sub-section (1) of section 36].

Provisions Relating to Accounts and Audit

4.15 Section 29 of the Act lays down requirements as to profit and loss account and balance sheet. Section 30 deals with audit of profit and loss account and balance sheet prepared in accordance with section 29. Section 31 deals with publication of profit and loss account and balance sheet and their submission toRBI, whereas section 32 deals with submission of profit and loss account and balance sheet to Registrar of Companies. Section 33deals with display of audited balance sheet and profit and loss account by companies incorporated outside India and carrying on banking business in India. It may be noted that some of the above provisions are not applicable to nationalized banks, State Bank of India, subsidiaries of State Bank of India, regional rural banks, and co-operative banks.

Other Important Provisions of the Banking Regulation Act, 1949

4.16 Besides the above provisions, a number of other provisions of the Act are relevant to the work of the auditor. Some of the important, provisions are:

Section 9	Disposal of non-banking assets(Banks are prohibited to hold any immovable property, other than assets for its own use and should dispose off the assets held in satisfaction of claim within 7 years or ' such extended period as RBI allows.)
Section 13	Restriction on commission, brokerage, discount and remuneration etc., on issue of shares up to 2.5 % of the paid up value of the shares
Section 14	Prohibition of charge on unpaid capital
Section 15	A banking company is prohibited from paying dividend unless expenses representing intangible assets are written off subject to exceptions provided
Section 17	Creation of Reserve fund
Section 18	Cash reserve to be maintained
Section 19	Restriction on nature of business of subsidiary Companies
Section 20	Restrictions on loans and advances
Section 20	A Restrictions on power to remit debts owed by directors and related enterprises
Section 21	Power of Reserve Bank to control advances by banking companies
Section 24	Maintenance of a percentage of *(liquid)* assets
Section 25	Quarterly return of Assets in India
Section 26	Return of unclaimed deposits (including non-operative accounts being older than 10 years or more)
Section 45Y	Power of Central Government to make rules for the preservation of records

Applicability of Various Enactments to Different Types of Banks

4.17 As mentioned in first paragraph, a number of enactments govern the functioning of banks in India. While the Banking Regulation Act, 1949 is applicable to all types of banks(though some of its provisions may not be applicable to certain types of banks or may be applicable with certain modifications), the other enactments are relevant only to particular type(s) of banks. The enactments applicable to different types of banks are discussed below:

Nationalized Banks

4.18 Nationalized banks are governed by:

(a) Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970/1980; and

(b) Specified provisions of the Banking Regulation Act, 1949.

4.19 Fourteen banks were nationalized under the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970while another six were nationalized under the Banking Companies(Acquisition and Transfer of Undertakings) Act, 1980. The provisions of these two enactments are identical and deal, *interalia,* with such matters as the following:

- Authorized and paid-up capital
- Annual accounts
- Qualifications, appointment, powers and duties of auditor (including contents of audit report)
- Disposal of profits
- Special audit at the instance of the Central Government
- Time and place of annual general meeting and business tobe transacted thereat
- Restrictions on payment of bonus to officers and other Employees
- Powers of the Board of Directors to make regulations in consultation with the RBI and with the previous sanction of the Central Government

4.20 Apart from all the provisions of the aforesaid Act of1970/1980, the following provisions of the Banking Regulation Act,1949, also apply to nationalized banks by virtue of section 51 of the later Act:

Section 10	Prohibition of employment of managing agents and restrictions on certain forms of employment

Section 13	Restriction on commission, brokerage, discount, etc., on sale of shares
Section 14	Prohibition of charge on unpaid capital
Section 14A	Prohibition of floating charge on assets
Section 15	Restrictions as to payment of dividend.
Section 17	Reserve Fund
Section 19	Restriction on nature of subsidiary companies
Section 20	Restrictions on loans and advances
Section 20A	Restriction on power to remit debts
Section 21	Power of RBI to control advances by banking Companies
Section 21A	Rate of interest charged by banking companies not to be subject to scrutiny by Courts
Section 23	Restrictions on opening of new, and transfer of existing, places of business
Section 24	Maintenance of a percentage of assets
Section 25	Assets in India
Section 26	Return of unclaimed deposits
Section 27	Monthly returns and power to call for other returns and information
Section 28	Power to publish information
Section 29[excluding sub-section (3)]	Accounts and balance sheet
Section 30[excluding sub-section (1) (1A) and (3)]	Audit
Section 31	Submission of returns

Section 34	Accounting provisions of the Act Not Retrospective
Section 35	Inspection
Section 35A	Power of the RBI to give directions
Section 36[excluding Clause D of sub-section (1)]	Further powers and functions of RBI.
Section 45Y	Power of Central Government to make rules for the preservation of records
Section 45Z	Return of paid instruments to customers
Section 45ZA	Nomination for payment of depositors 'Money
Section 45ZB	Notice of claims of other persons regarding deposits not receivable
Section 45ZC	Nomination for return of articles kept in safe custody with banking company
Section 45ZD	Notice of claims of other persons regarding articles not receivable
Section 45ZE	Release of contents of safety lockers
Section 45ZF	Notice of claims of other persons regarding safety lockers not receivable
Section 46	Penalties
Section 46A	Chairman, director, etc., to be public servants for the purposes of Chapter IX of the Indian Penal Code
Section 47	Cognizance of offences
Section 47A	Power of RBI to impose penalty
Section 48	Application of fines
Section 50	Certain claims for compensation barred
Section 52	Power of Central Government to make rules
Section 53	Power to exempt in certain cases

State Bank of India and its Subsidiaries

4.21 State Bank of India and its subsidiaries are governed by:

(a) State Bank of India Act, 1955/State Bank of India (Subsidiary Banks) Act, 1959, as the case may be; and

(b) Specified provisions of the Banking Regulation Act, 1949.

4.22 The provisions of the Banking Regulation Act, 1949, applicable to State Bank of India and its subsidiaries are specified in section 51 of the said Act and are the same as those applicable to nationalized banks.

Banking Companies

4.23 Section 2 of the Banking Regulation Act, 1949, provides that the provisions of the Act shall be in addition to, and not, save as expressly provided there under, in derogation of the Companies Act, 1956, and any other law for the time being in force. Thus, banking companies attract the provisions of both the Banking Regulation Act, 1949, as well as the Companies Act, 1956. In case the provisions of these enactments are at variance, the provisions of the Banking Regulation Act, 1949, shall prevail.

Regional Rural Banks

4.24 Regional rural banks are governed by

(a) Regional Rural Banks Act, 1976; and

(b) Specified provisions of the Banking Regulation Act, 1949.

4.25 The provisions of the Banking Regulation Act, 1949, applicable to regional rural banks are specified in section 51 of the said Act and are the same as those applicable to nationalized banks.

4.26 Each 'RRB' has a public sector bank as its sponsor bank. The capital of 'RRB' is contributed by the Central Government, State Government & the Sponsor Bank in proportion of 50%,15% and 35% respectively.

Co-operative Banks

4.27 Co-operative banks are governed by:

(a) the Co-operative Societies Act, 1912, or the Co-operative Societies Act of the state concerned, as the case may be; And

(b) Part V of the Banking Regulation Act, 1949.

4.28 Part V of the Banking Regulation Act, 1949, modifies certain provisions of the Act in their application to co-operative banks and omits certain others. The sections which have been significantly modified in their application to co-operative banks are sections 2, 5-A, 8, 9, 11, 18, 19, 20, 22, 23, 24, 27, 29, 31, 35,35A, 36, 36A, 49A, 54 and 55. Besides, the First Schedule to the Act is not applicable to co-operative banks while the Third and the Fourth Schedules to the Act have been replaced by a schedule applicable only to co-operative banks.

Scheduled Banks

4.29 These are the banks included in the Second Schedule to the Reserve Bank of India Act, 1934. The Reserve Bank includes a Bank in this Schedule, if it fulfils certain conditions.

4.30 The Reserve Bank gives certain facilities to scheduled banks including the following:

(a) Purchase, sale and rediscounting of certain bills of exchange (including foreign bills of exchange) or promissory notes.

(b) Purchase and sale of foreign exchange.

(c) Making of loans and advances to scheduled banks.

(d) Maintenance of the accounts of scheduled banks in its banking department and issue department.

(e) Remittance of money between different branches of scheduled banks through the offices, branches or agencies of the Reserve Bank free of charge or at nominal charges.

Returns to be Submitted to the RBI

4.31 The Banking Regulation Act, 1949 requires banking companies, nationalized banks, State Bank of India, its subsidiaries, and regional rural banks to furnish the following returns to the RBI:

(a) Monthly return of assets maintained in India in accordance with section 24 and demand and time liabilities in India at the close of business on each alternate Friday during the month. [Section 24]

(b) Quarterly return of assets and liabilities in India at the close of business on the last Friday of every quarter. [Section 25]

(c) Annual return of unclaimed accounts which have not been operated for 10 years. [Section 26]

(d) Monthly return of assets and liabilities in India at the close of business on the last Friday of every month. [Section 27]

4.32 The above types of banks have also to furnish such other statements or information as may be required by the RBI under section 27 of the Act. In exercise of its powers under the aforesaid section, the RBI requires a large number of returns to be furnished to it. Some of the important returns required to be furnished to the RBI are as enumerated below, with their periodicity indicated in parentheses:

(a) Report on Non-Performing Advances (annual)

(b) Statement showing the position of reconciliation of investment account (annual)

(c) Statement on compromises and settlements involving write-off (half yearly)

(d) Statement on bad debts written off (annual)

(e) Details of Doubtful or Loss Assets and also Suit Filed accounts with outstanding aggregating ₹1crore and above(half-yearly)

(f) Details of remittance of profits / surplus retained in India(annual)

(g) Particulars of provisions held on problem credits of overseas branches (half-yearly)

(h) Inter-branch reconciliation (quarterly)

(i) Reconciliation of outstanding inter-branch accounts (annual)

(j) Reconciliation of clearing differences (annual)

(k) Position of balancing of books (quarterly)

(l) Returns relating to frauds, robbery, etc. including fraud involving` one crore and above (quarterly)

(m) Return of Capital Adequacy (quarterly)

(n) Return on Asset Quality (quarterly)

(o) Asset-liability management (monthly)

(p) Return in respect of Statutory Liquidity Ratio (monthly)

Online Reporting to RBI through 'ORFS' and 'XBRL'.

4.33 As a regulatory and supervisory function bestowed on RBI, it collects returns from commercial banks, financial institutions, etc. Many of these returns are the statutory requirement under Reserve Bank of India Act ,1934, Banking Regulation Act,1949, FEMA ,1990.

4.34 The conventional method of return submission requires sending of hard copy through postal services, fax and PDF file through e-mail. All these modes of filing returns have their own limitations. Hence, the need was felt for developing the single electronic return submission window 'ORFS' (Online Filing System).

4.35 As a part of online filing of returns, the Reserve Bank of India felt the need for the adoption of best internet technology solution. Thus, RBI has adopted 'XBRL' (extensible Business Reporting Language) which attends the standardization of business reporting especially Financial Reporting. While 'ORFS' brings no standardization across all the returns, 'XBRL' is capable of implementing global standards across all returns. Today, these two online systems, i.e., 'ORFS' and 'XBRL' coexists with conventional form of return submission.

Chapter 5
PMLA and Know Your Customer (KYC) Policy

Introduction

5.1 RBI has issued "Master Direction – Know Your Customer (KYC) Direction, 2016" on February 25, 2016 which has been updated on July 8, 2016. All earlier circulars issued on this subject are repealed with the issuance of this Master Direction. Summarized and simplified version of Reserve Bank of India's Know Your Customers' guidelines are appended at the end of this chapter which are updated upto 02-09-2016.

As per "Master Direction-Know Your Customer (KYC), Directions 2016", the provisions of Prevention of Money-Laundering Act (PMLA), 2002 and the Prevention of Money Laundering (Maintenance of Records) Rules, 2005, Regulated Entities (REs)* are required to follow certain customer identification procedures while undertaking a transaction either by establishing an account based relationship or otherwise and monitor their transactions. Accordingly, in exercise of the powers conferred by section 35A of the Banking Regulation Act, 1949, read with section 56 of the Act ibid and Rule 9(14) of Prevention of Money Laundering (Maintenance of Records) Rules, 2005, the Reserve Bank of India being satisfied that it is necessary and expedient in the public interest to do so, hereby issues directions on KYC.

[*Regulated Entities (REs) means all Scheduled Commercial Banks (SCBs), RRBs / Local Area Banks/ All Primary (Urban) Co-operative Banks/ State and Central Co-operative Banks and any other entity licensed u/s 22 of the Banking Regulation Act, 1949.]

5.2 Offence of Money Laundering is defined in Section 3 of Prevention of Money Laundering Act (PMLA) 2002, which states that whosoever directly or indirectly attempts to indulge or knowingly assist or knowingly is a party or is actually involved in any process or activity connected with the proceeds of crime and projecting it as untainted property shall be guilty of offence of money laundering.

Further, The Prevention of Money Laundering (Amendment) Act, 2012, has amended that in Section 3 for the words “proceeds of crime and projecting”' the words “proceeds of crime including its concealment, possession, acquisition or use and projecting or claiming” shall be substituted.

5.3 ‘Money Laundering’ is, therefore, an activity which involves washing and ironing illegal/ black earning as legitimate / white earning. In other words, money generated from illegitimate sources is converted into that derived from legitimate source and is called money laundering. Whereas ‘Terrorist Financing’ is the reverse procedure of money laundering. Here the money earned from legitimate sources is used for illegitimate activities, i.e., financing terrorism.

Objective

5.4 KYC refers to the policies and procedures established by the Banks, Intermediaries and Financial Institutions (BIF) to ensure that bank system is not used by malafide people and criminal elements for money laundering activities. Objective of KYC Policy is that due care should be taken before any business relationship is entered. This involves verifying customer’s identity and address, by asking them to submit documents that are accepted as relevant proof.

5.5 Banks have been advised to follow certain customer identification procedure for opening of account and monitoring transactions of suspicious nature for the purpose of reporting it to appropriate authority. Banks have been advised to ensure that a proper policy framework on KYC and AML measures is to be formulated and put in place, with the approval of the Board of Directors of ‘Regulated Entities (REs) or any committee of the Board to which power has been delegated.

Framing of KYC Policy

5.6 KYC is a framework for banks which enables them to know/ understand the customers and their financial dealings. Key elements of KYC Policies are as follows:

(a) ***Customer Acceptance Policy(CAP)-*** It is the criteria for either entering into and maintaining customer relationship or terminating the same. All banks shall develop criteria for accepting any person as their customer to restrict any anonymous or fictitious or benami account and ensure documentation mentioned in KYC policy. Banks shall not open an account where the Regulated Entity is unable to apply appropriate customer due diligence measure, i.e., bank is unable to verify the identity and/ or obtain required documents either due to non-cooperation or due to non-reliability of documents/ information furnished by the customers. Customer Acceptance Policy shall not result in denial of banking / financial facility to members of the general public, especially those, who are financially or socially disadvantaged

(b) ***Risk Management*** **-** Regulated Authorities (REs) shall have a risk based approach which includes the following:

(i) Customers shall be categorized as low, medium and high risk category based on its assessment and risk perception of the Regulated Authorities.

(ii) Risk categorization shall be undertaken based on parameters such as customer's identity, social/ financial status, nature of business activity, nature of business and location, etc.

Provided that various other information's collected from different categories of customers relating to perceived risk, is a non-intrusive and the same is specified in the KYC Policy.

It is clarified that FATF Public Statements, the reports and guidance notes on KYC / AML issued by Indian Bank Association, guidance note circulated to all co-operative banks by RBI etc. may also be used in risk assessment.

(c) ***Customer Identification Procedure (CIP)*** **-** It is the procedure to be carried out while establishing a banking relationship or carrying out a financial transaction. Requirement to obtain customer identification lies in case of existing customers as well as when the bank has a doubt about the authenticity or the adequacy of the previously obtained customer identification data.CIP is also required where REs carry out transactions for a non-account based customer, i.e., a walk in customers where amount is ₹ 50,000/- or more, whether conducted as a single transaction or several transactions that appear to be connected, etc. Further, when a RE has reason to believe that a customer (account-based or walk-in) is intentionally structuring a transaction into a series of transaction below the threshold limit of ₹ 50000/-

For the purpose of verifying the identity of customers at the time of commencement of an account based relationships, REs shall at their option, rely on customer due diligence done by a third party.

(d) ***Monitoring of Transactions-*** Key points to be considered are as follows:

(i) Banks are advised to monitor transactions which exceed the 'thresholds' prescribed for specific category of accounts.

(ii) Banks are advised to set key indicators for risk sensitive accounts (e.g., high turnover accounts or complex or unusual transactions accounts).

(iii) Banks are also advised to take note of the background of the customer (e.g., country of origin, sources of funds, types of transaction involved and other risk factors).

(iv) Banks should also put in place a system of periodical review of risk categorization of accounts and the need for applying enhanced due diligence measures. Such review of risk categorization of customers should be carried out at a periodicity of not less than once in a six months.

(v) In case of non-application of proper KYC measures, banks may decide to close the account of the particular customer after giving due notice to the customer.

Requirements under PMLA, 2002

5.7 Chapter IV of PMLA, 2002 read with The Prevention of Money Laundering (Amendment) Act, 2012, deals with the obligation of reporting entities, i.e., Banking Companies, Financial Institutions and Intermediaries under the above Act which are as follows:

(i) Section 12 requires reporting entities to maintain records of all transactions in such a manner as to enable to reconstruct individual transactions; furnishing the above information to the directors; verify the identity of the clients; and maintain records of documents evidencing identity of clients and beneficial owners.

(ii) Section 12 A is a new section inserted by PML (Amendment) Act, 2012, which provides access to information to the directors who may call for, from any reporting entities, any of the records maintained under sub section (1) of Section 12 or any other additional information and such reporting authority has to furnish such information asked for.

(iii) Section 13 empowers the directors of reporting entity, to make such enquiry or cause such inquiry to be made as he thinks fit to be necessary, with regards to obligations of the reporting entity.

(iv) Section 14 provides the protection to reporting entity and its officers from any liability in civil proceedings for providing information required under section 12. Now, by PML (Amendment) Act, 2012, criminal liability also added in above section.

(iv) Section 15 deals with manner of furnishing of information to the directors by the reporting entity (BIF).

5.8 Definition of Reporting Entity, Banking Companies, Intermediaries and Financial Institutions, are as follows:

Reporting Entity means a banking company, financial institutions, intermediary or a person carrying on a designated business or profession.

Banking Companies has been defined in section 2(e) of the Act which means a banking company or a co-operative bank to which Banking Regulation Act, 1949 applies and includes any bank or banking institution referred to in section 51 of that Act. Further, Section 5 (b) of the Banking Regulations Act, 1949 defines 'banking as accepting for the purpose of lending or investment, of deposits of money from the public, repayable on demand or 'otherwise and withdrawal by cheques, drafts, order or otherwise.

Intermediary as per Section 2(n) of the Act (amended by The Prevention of Money Laundering (Amendment) Act, 2012) means:

(i) a stock broker, sub-broker, share transfer agent, bankers to an issue, trustee to a trust deed, registrar to an issue, merchant bankers, underwriters, portfolio managers, investment adviser or any other intermediary associated with securities market and registered under section 12 of the Securities and Exchange Board of India Act, 1992 or

(ii) An association recognized or registered under the Forward Contracts (Regulations) Act, 1952 or any member of such association; or

(iii) Intermediary registered by the Pension Fund Regulatory and Development Authority; or

(iv) A recognized stock exchange referred to in clause (f) of section 2 of the Securities Contracts (Regulation) Act, 1956.

Financial Institution has been defined under section 2(**l**) of the Act to mean a financial institution as defined in clause (c) of section 45-I of the Reserve Bank of India Act, 1934and includes a chit fund company, a housing finance institution, an authorized person, a payment system operator, a non-banking financial company and the Department of Posts in the Government of India..

Important Rules Prescribed Under PMLA, 2002

5.9 Prevention of Money-laundering (the Manner of forwarding a copy of the Order of Provisional Attachment of Property along with the Material, and copy of the Reasons along with the Material in respect of Survey, to the Adjudicating Authority and its period of Retention) Rules, 2005, *inter alia* provides following definitions:

(a) ***Suspicious Transactions*****(Rule 2(1g))**:

It is defined as transaction whether or not made in cash, which to a person acting in good faith-

(i) give rise to a reasonable ground of suspicion that it may involve proceeds of crime ;or

(ii) appears to be made in circumstances of unusual or unjustified complexity ;or

(iii) appears to have no economic, rational or bonafide purpose.

(b) ***Maintenance of Records of Transactions (Nature and Value)*** **Rule 3(1)**:

Every banking company or financial institution or intermediaries, as the case may be,' shall maintain a record of:

(i) all cash transactions of the value of more than ₹ ten lakhs or its equivalent in foreign currency.

(ii) all series of cash transactions integrally connected to each other taking place in a month exceeding limit of rupee ten lakhs.

(iii) all cash transactions were forged or counterfeit currency notes or bank notes have been used as genuine or where any forgery of a valuable security has taken place.

(iv) all suspicious transactions whether or not made in cash (as listed in such clause (i) to (v) of above rule) like, cheque, transfer, demat account, money transfer, loans and advances, etc.

***(c) Records Containing Information*(Rule 4)**:

Such records should describe:

(i) nature of the transaction;

(ii) amount and currency of transaction

(iii) date of the transaction

(iv) parties to the transaction

***(d) Procedure and Manner of Maintaining Information*(Rule 5):**

(i) In 'Hard' and 'Soft' copy in accordance with the procedure as specified by RBI and SEBI.

(ii) Evolve an internal mechanism to keep these records as per RBI and SEBI guidelines.

(iii) Follow the procedure and manner of maintaining information as specified by RBI and SEBI.

***(e) Retention of Records*(Rule 6)**:

It requires 'BIF' to maintain the records as required by these rules for ten years after the date of cessation of transaction between the BIF and the client.

***(f) Time Limit of Furnishing Records to the director*(Rule 8):**

(i) In case of transaction exceeding the specified limit, within 7 days of end of the month in which they occur.

(ii) In case of forged currency or security transaction and suspicious transactions, within 3 days of transaction.

(g) *Verification of the Records for the Identity of Clients*(Rule 9):

(i) Records to be procured at opening of an account:

Sub-rule 1 of Rule 9 requires that at the time of opening of an account of every client, the bank shall procure-

- Records of identity of the client
- Current address and permanent address
- Nature of business and his financial status

(ii) Records to be submitted by client:

Sub Rule 2 to 6 of Rule 9requires documents like-

- 'officially valid documents', containing details of his permanent address, current address
- one recent photograph,
- Proof of nature of business and the financial status.

(iii) *Officially valid documents* has been defined under Rule 2(1)(d) which includes:

- Pass port or
- The Driving license or
- The PAN or
- The Voter ID Card or
- Any other document as may be required by the BIF, of the client.

(For Example: Where the client is company- Certificate of Incorporation, MOA, AOA, Resolution of board of directors etc. and where the client is a partnership firm - Partnership deed, registration certificate, etc.)

(iv) Client Identification Programme:

Sub-rule 7 of Rule 9 requires that every BFI shall formulate and implement a client identification programme which shall incorporate the given requirements and such other things as may be considered appropriate to enable it to determine true identity of its clients. A copy of the program is to be forwarded to the directors.

(v) *Maintenance of Records of Identity of Client*

Rule 10 contains requirements similar to that of Rule 6 but in respect of records relating to the identity of the client instead of that relating to the transaction.

Further, as per Rule 7 (1) of Prevention of Money Laundering (Maintenance of Records) Rules, 2005, appointment of designated director and compliance officer is to be made for implementation of AML Act provisions. Definition of designation director is given in sec 2 (1) (ba)

Reporting Requirement of Cash and Suspicious Transaction to Financial Intelligence Unit-India (FIU-IND)

5.10 Reporting Entities (REs) shall furnish to the Director, Finance Intelligence Unit-India (FIU-IND), information referred to in Rule 3 of PML (Maintenance of Records) Rules, 2005 in terms of Rule 7. The reporting formats and comprehensive reporting format guide released by FIU-IND and Report Generation Utility and Report Validation Utility developed to assist reporting entities in the preparation of prescribed reports. These reports include Cash Transaction Reports (CTR) / Suspicious Transaction Reports (STR) which WIV-IND has placed on website.

(a) Cash Transaction Report (CTR)

(i) CTR of each month should be submitted to FIU-IND by 15thof succeeding month. Cash Transaction reporting by branches to its controlling office should be submitted on monthly basis so that bank should ensure its compliance.

(ii) All cash transactions where forged or counterfeit Indian currency notes have been used as genuine should be reported by 15th of next month. These cash transactions should also include transactions where forgery of valuable security or documents has taken place.

(iii) CTR cut off limit is of ₹ 10 Lakhs or its equivalent in foreign currency.

(iv) All series of cash transactions integrally connected to each other which are valued below ₹ 10 Lakhs or its equivalent in foreign currency where such series of transactions have been taken place within a month.

(v) CTR should contain only the transactions carried out by bank on behalf of their clients / customers only.

(b) Suspicious Transaction Report (STR)

(i) While determining suspicious transaction, bank should be guided by the definition of "Suspicious Transaction" as contained in PMLA Rules.

(ii) In some cases, where transaction is abandoned by customers, on being asked some details or provide some documents, such attempted transactions should also be reported.

(iii) Bank should make STR if they have reasonable ground of believe that the transaction involves proceeds of crime, irrespective of amount of transaction etc.

(iv) Bank should put in place an appropriate software application to through alerts and transactions are inconsistent with his categorization and updated profile of customers.

(v) STR should be furnished within 7 days of arriving at a conclusion that such a transaction is of suspicious nature.

Types of Suspicious Transactions

5.11 Following are some common types of suspicious transactions:

(i) Transactions involving large amount of cash.

For example: large cash deposits into same account, substantial increase in turnover in a dormant account.

(ii) Activities not consistent with the customer business.

For example: Accounts with large volume of credits whereas nature of business is not so much fixed.

(iii) Transactions that do not make economic sense.

For example: Transaction in which assets are withdrawn immediately after being deposited.

(iv) Attempts to avoid reporting / record keeping requirement.

For example: A customer who is reluctant to provide information needed for a mandatory report, where customer splits the transaction into similar amount to avoid the threshold limit.

(v) Unusual activities

For example: Funds are coming from countries/ centers which are instrumental for money laundering.

(vi) Provide insufficient or suspicious Information

For example:

(a) A customer who is reluctant to provide complete information regarding the purpose of business, location, directors etc.

(b) A customer who do not provide ' Financial Statements'

(c) A customer who has no record of employment but makes frequent large transactions.

(vii) Employees Arousing Suspicion

For example: An employee whose lavish lifestyle cannot be supported by his salary.

(a) Negligence of an employee/ willful blindness is reported repeatedly.

Annexure I

Know Your Customer Guidelines

(Updated up to September 02, 2016)

(This is a summarised and simplified version of the Reserve Bank of India's Know Your Customer guidelines.)

(Refer RBI website www.rbi.org.in)

Q1. What is KYC? Why is it required?

Response: KYC means "Know Your Customer". It is a process by which banks obtain information about the identity and address of the customers. This process helps to ensure that banks' services are not misused. The KYC procedure is to be completed by the banks while opening accounts. Banks are also required to periodically update their customers' KYC details.

Q2. What are the KYC requirements for opening a bank account?

Response: To open a bank account, one needs to submit a 'proof of identity and proof of address' together with a recent photograph.

Q3. What are the documents to be given as 'proof of identity' and 'proof of address'?

Response: The Government of India has notified six documents as 'Officially Valid Documents' (OVDs) for the purpose of producing proof of identity. These six documents are Passport, Driving License, Voters' Identity Card, PAN Card, Aadhaar Card issued by UIDAI and NREGA Job Card. You need to submit any one of these documents as proof of identity. If these documents also contain your address details, then it would also be accepted as 'proof of address'. If the document submitted by you for proof of identity does not contain address details, then you will have to submit another officially valid document which contains address details.

Q4. If I do not have any of the documents listed above to show my 'proof of identity', can I still open a bank account?

Response: Yes. You can still open a bank account known as 'Small Account' by submitting your recent photograph and putting your signature or thumb impression in the presence of the bank official.

Q5. Is there any difference between such 'small accounts' and other accounts

Response: Yes. The 'Small Accounts' have certain limitations such as:

- balance in such accounts at any point of time should not exceed ₹50,000
- total credits in one year should not exceed ₹1,00,000
- total withdrawal and transfers in a month should not exceed ₹10,000
- Foreign remittances cannot be credited to such accounts.

Such accounts remain operational initially for a period of twelve months and thereafter, for a further period of twelve months if the holder of such an account provides evidence to the bank of having applied for any of the officially valid documents within twelve months of the opening of such account.

Q6. Would it be possible, if I do not have any of the officially valid documents, to have a bank account, which is not subjected to any limitations as in the case of 'small accounts'?

Response: A normal account can be opened by submitting a copy of any one of the following documents as Proof of Identity (PoI):

(i) Identity card with person's photograph issued by Central/State Government Departments, Statutory/Regulatory Authorities, Public Sector Undertakings, Scheduled Commercial Banks, and Public Financial Institutions;

or

(ii) letter issued by a gazetted officer, with a duly attested photograph of the person.

For Proof of Address (PoA), you may submit the following documents:

(i) Utility bill, which is not more than two months old, of any service provider (electricity, telephone, post-paid mobile phone, piped gas, water bill);

(ii) Property or Municipal Tax receipt;

(iii) Bank account or Post Office savings bank account statement;

(iv) Pension or family Pension Payment Orders (PPOs) issued to retired employees by Government Departments or Public Sector Undertakings, if they contain the address;

(v) Letter of allotment of accommodation from employer issued by State or Central Government departments, statutory or regulatory bodies, public sector undertakings, scheduled commercial banks, financial institutions and listed companies. Similarly, leave and license agreements with such employers allotting official accommodation; and

(vi) Documents issued by Government departments of foreign jurisdictions or letter issued by Foreign Embassy or Mission in India.

This, however, is not a general rule and it is left to the judgment of the banks to decide whether this simplified procedure can be adopted in respect of any customer.

Q7. If my name has been changed and I do not have any OVD in the new name, how can I open an account?

Response: A copy of the marriage certificate issued by the State Government or Gazette notification indicating change in name together with a certified copy of the 'Officially Valid Documents' in the prior name of the person is to be furnished for opening of account in cases of persons who change their names on account of marriage or otherwise.

Q8. Are banks required to categories their customers based on risk assessment?

Response: Yes, banks are required to classify their customers into 'low', 'medium' and 'high' risk categories depending on their AML risk assessment.

Q9. Do banks inform customers about this risk categorization?

Response: No

Q10. If I refuse to provide requested documents for KYC to my bank for opening an account, what may be the result?

Response: If you do not provide the required documents for KYC, the bank will not be able to open your account.

Q11. Can I open a bank account with only an Aadhaar card?

Response: Yes, Aadhaar card is accepted as a proof of both identity and address.

Q12. Is it compulsory to furnish Aadhaar Card for opening an account?

Response: No. you may furnish Aadhaar card or any of the other five OVDs for opening an account.

Q13. What is e-KYC? How does e-KYC work?

Response: e-KYC refers to electronic KYC.

e-KYC is possible only for those who have Aadhaar numbers. While using e-KYC service, you have to authorize the Unique Identification Authority of India (UIDAI), by explicit consent, to release your identity/address through biometric authentication to the bank branches/business correspondent (BC). The UIDAI then transfers your data comprising your name, age, gender, and photograph electronically to the bank. Information thus provided through e-KYC process is permitted to be treated as an 'Officially Valid Document' under PML Rules and is a valid process for KYC verification.

Q14. Is introduction necessary while opening a bank account?

Response: No, introduction is not required.

Q15. If I am staying in Chennai but if my proof of address shows my address of New Delhi, can I still open an account in Chennai?

Response: Yes. You can open a bank account in Chennai even if the address in the "Officially Valid Document" is that of New Delhi and you do not have a proof of address for your Chennai address. In such case, you can submit the officially valid document having your New Delhi address, together with a declaration about your Chennai address for communication purposes.

Q16. Can I transfer my existing bank account from one place to another? Do I need to undergo full KYC again?

Response: It is possible to transfer an account from one branch to another branch of the same bank. There is no need to undergo KYC exercise again for such transfer. However, if there is a change of address, then you will have to submit a declaration about the current address. If the address appearing in the 'Officially Valid Documents' (OVDs) submitted for proof of address is no longer your valid address (i.e. neither your permanent address nor your current address), you need to get an Officially Valid Document for Proof of Address containing the current or the permanent address and furnish the same within six months. In case of opening an account in another bank, however, you will have to undergo KYC exercise afresh.

Q17. Do I have to furnish KYC documents for each account I open in a bank even though I have furnished the documents of proof of identity and address?

Response: No, if you have opened a KYC compliant account with a bank, other than a 'small account', then for opening another account with the same bank, furnishing of documents is not necessary.

Q18. For which banking transactions do I need to quote my PAN number?

Response: PAN number needs to be quoted for transactions such as account opening, transactions above ₹50,000 (whether in cash or non-cash), etc. A full list of transactions where PAN number needs to be quoted can be accessed from website of Income Tax Department at the following URL: http://www.incometaxindia.gov.in/_layouts/15/dit/pages/viewer.aspx?grp=rule&cname=CMSID&cval=103120000000007541&searchFilter=&k=114b&IsDlg=0

Q19. Whether KYC is applicable for Credit/Debit cards?

Response: Yes. KYC exercise is necessary for Credit/ Smart Cards and also in respect of add-on/ supplementary cards. Since debit cards are issued only to account holders and accounts are opened only after the KYC procedure is completed, there is no need for separate KYC for issuing debit card.

Q20. I do not have a bank account. But I need to make a remittance. Is KYC applicable to me?

Response: Yes. KYC exercise needs to be done for all those who want to make domestic remittances of ₹ 50,000 and above and all foreign remittances.

Q21. Can I purchase a Demand Draft/Payment Order/Travelers Cheque against cash?

Response: Yes, Demand Draft/Payment Order/Travelers Cheques for below ₹50,000/- can be purchased against cash and such instruments for ₹ 50000/- and above can be issued only by way of debiting the customer's account or against cheques.

Q22. Do I need to submit KYC documents to the bank while purchasing third party products (like insurance or mutual fund products) from banks?

Response: Yes, all customers who do not have accounts with the bank (known as walk-in customers) have to produce proof of identity and address while purchasing third party products from banks if the transaction is for ₹50,000 and above. KYC exercise will not be necessary for bank's own customers for purchasing third party products. However, instructions to make payment by debit to customers' accounts or against cheques for remittance of funds/issue of travelers' cheques, sale of gold/silver/platinum and the requirement of quoting PAN number for transactions of ₹50,000 and above will be applicable to purchase of third party products from bank by its customers as also to walk-in customers.

Q23. My KYC was completed when I opened the account. Why does my bank insist on doing KYC again?

Response: Banks are required to periodically update KYC records. This is a part of their ongoing due diligence on bank accounts. The periodicity of such updation varies from account to account depending on its risk categorization by the bank. Periodic updation of records also helps prevent frauds in customer accounts.

Q24. What are the rules regarding periodic updation of KYC?

Response: Different periodicities have been prescribed for updation of KYC records depending on the risk perception of the bank. KYC is required to be done at least once in two years for high risk customers, once in eight years for medium risk customers and once in ten years for low risk customers. This exercise would involve all formalities for KYC normally taken at the time of opening the account.

While periodic updation of KYC has to be carried out in respect of customer categorised as 'low risk' also, if there is no change in status with respect to the identity (change in name, etc.) and/or address of such customers the banks may ask such customers to submit only a self-certification about 'no-change in status' at the time of periodic updation. Banks may not ask such customers to submit copies of 'Officially Valid Documents' for periodic updation.

In case of change of address of such 'low risk' customers, they could merely forward a certified copy of the document (proof of address) by mail/post, etc. Physical presence of such low risk customer is not required at the time of periodic updation.

Customers who are minors have to submit fresh photograph on becoming major.

Q25. What if I do not provide the KYC documents at the time of periodic updation?

Response: If you do not provide your KYC documents at the time of periodic updation, bank has the option to close your account. Before closing the account, the bank may, however, impose 'partial freezing' (i.e. initially allowing all credits and disallowing all debits while giving an option to you to close the account and take your money back). Later, even credits also would not be allowed. The 'partial freezing' however, would be exercised by the bank after giving you due notice.

Q26. How is partial freezing imposed?

Response: Partial freezing is imposed in the following ways:

- Banks have to give due notice of three months initially to the customers before exercising the option of 'partial freezing'.
- After that a reminder for further period of three months will be issued.
- Thereafter, banks shall impose 'partial freezing' by allowing all credits and disallowing all debits with the freedom to close the accounts.
- If the accounts are still KYC non-compliant after six months of imposing initial 'partial freezing' banks shall disallow all debits and credits from/to the accounts, classifying them inoperative.

Meanwhile, the account holders can revive accounts by submitting the KYC documents.

Chapter 6
Internal Control, Inspection and Internal Audit

Internal Control

6.1 The system of internal control is devised by anorganization in order to achieve management's objectives. It constitutes all the methods and procedures which are adopted by the management of an entity in ensuring, as far as possible, orderly and efficient conduct of its business, including adherence to management policies, safeguarding assets through prevention and detection of errors and fraud, ensuring accuracy, completeness of the accounting records and the timely preparation of the reliable financial information are the basic objectives of a sound internal control system. The system of internal control extends beyond those matters which directly relate to the functions of the Banking systems. The functions are classified as under:

- Credit Function
- Non Credit Function
- Computer functions
- Compliance Functions
- Branch Management.

Internal control procedures of a bank, generally, fall under the following categories:

(i) Delegation of powers

(ii) Authorization of transactions

(iii) Segregation and rotation of duties

(iv) Maintenance of adequate records and documents

(v) Accountability for and safeguarding of assets

(vi) System configuration and account mapping

(vii) Independent checks

(viii) Identification of Customer

(ix) Internal control in respect of various functions are:

(a) CREDIT FUNCTIONS

- Exercise of Loaning Powers.
- Pre sanction Appraisal.
- Documentation
- Creation of Charges
- Creation of Mortgage
- Post Sanction monitoring and follow up.
- Non fund based limits scrutiny and proper treatment of its reversal.
- FOREX functions- whether as per FEMA guidelines and banks internal procedure.

(b) NON CREDIT FUNCTIONS

- Balancing
- Cash Management.
- Currency Chest
- Remittance in transit
- ATM
- Bankers account and clearing.
- Suspense and sundries.
- Daily monitoring system.
- Account opening and KYC.
- Conduct and Maintenance of accounts.
- Security forms inventory.
- Bills for Collection/Demand draft.
- Government Business.
- Safe deposit vault.
- Customer service.

(c) COMPUTER FUNCTIONS

- Environmental Controls.
- Physical and Logical Controls
- Maintenance and Business controls.
- Network Control.
- Operational Control.

(d) COMPLIANCE FUNCTIONS

- Inspection report.
- Return submission.
- Communication & response.
- Regulatory compliance.

(e) BRANCH MANAGEMENT FUNCTIONS

- General.
- Security.

Vigilance Function in Banks

6.2 All banks have a vigilance department, though it may be assigned different names in different banks. Its functions include surveillance over the suspect staff/ transactions, and also lookingin to cases of frauds/misappropriation/connivance, etc. leading to loss to the bank. In the case of large non-performing assets, the department may be required to investigate and detect the reason for the same. The nature of findings of the vigilance department is of relevance to the auditor, particularly in evaluating the efficacy of internal controls including the depth of preventing vigilance.

Inspection

Branch Inspection

6.3 Such inspection is much broader and covers all important areas of functioning, including efficacy of systems and procedures, compliance with head office directions, customer service, maintenance of books and records, etc. Most banks have a fixed schedule of branch inspection.

6.4 Besides the regular Inspection of branch inspection of big loan accounts are carried separately known as CARD Audit.

6.5 CA firms are also deployed to check revenue income and find out revenue loss if any at the branch level.

Head Office

Inspection

6.6 The inspection at head office level is aimed at evaluating the functions being carried out at the head office. It covers, *interalia*, investment and other treasury functions, functioning of the central stationery department, fixed assets (if centralized), inter branch reconciliation, etc.

RBI Inspection

6.7 The RBI also carries out inspection of branches under section 35 of the Banking Regulation Act, 1949, to examine compliance of various policies and norms about credit and other functions laid down by the RBI from time to time. Besides, the RBI also carries out inspection of currency chest branches to review chest balances and other functions that are being performed by the branches as its agent.RBI inspections, however, are not in the nature of internal audit.

Internal Audit Systems in Banks

Revenue Audit

6.8 Revenue audit is aimed at identifying cases of:

(i) leakage of revenue due to wrong computation of interest,

(ii) non-application of interest on time,

(iii) application of incorrect rates of interest,

(iv) not charging penal interest on overdue installments or late submission of stock statements or non-compliance of any other condition,

(v) non-charging of processing charges on renewal of limit,

(vi) non-recovery, short/ excess recovery of service charges on guarantees and letter of credit, etc,

(vii) non recovery, short/ excess recovery of processing charges and documentation fees,

(viii) non recovery, short/ excess recovery of inspection charges and other services charges,

(ix) non recovery, short/ excess recovery of commitment charges/ CIBIL charges.

6.9 As already stated, revenue audit exercise is to detect leakage of revenue, but this is not the sole purpose of this audit. Auditors are also required to examine the reasons for any leakage of revenue. A separate report for intentional mistakes of revenue leakage is annexed to the main report by the auditor. This type of audit is also known as income and expenditure audit and revenue/income leakage audit.

Stock and Receivable Audit

6.10 The essentials of this audit should not be confined, merely checking of physical existence of stocks and the book debts as appearing in the books of account (ledger balance) but would encompass a general over view of the borrowing unit's operation which can be summarized as under:

(i) To check whether the stocks are covered by adequate comprehensive insurance policies and ensure that 'the bank clause' has been specified in policy in terms of the sanction letter of the respective borrower.

(ii) To check whether stock statements are submitted in time and adequate details/location are there.

(iii) To check whether stock statements are duly scrutinized by bank officials

(iv) To check whether drawing power is calculated correctly and DP register is maintained upto date.

(v) To check quality of goods, in particular to detect the slow moving or non-moving goods etc. (insurance stock of stores to be identified)

(vi) To check validity of primary securities.

(vii) To check book-keeping whether updated.

(viii) To check system of stock receipts / issues and its reconciliation with physical quantity.

(ix) To check whether the stocks are in conformity with excise/ Vat/ service tax records, etc.

(x) To check Valuation of stocks including WIP, Finished Goods etc. and whether valuation is made as per AS-2 and also to ascertain how far they are reasonable based on the consistent practice followed.

(xi) Confirmation of the balances of book debts from the respective parties and also to ascertain whether age wise analysis of debtors is done.

(xii) To check whether certificate obtained from third party in respect of stocks lying with third party.

(xiii) To check whether goods of third parties lying with borrower are excluded to calculate drawing power.

(xiv) To check whether stock are physically verified by branch officer from time to time.

(xv) To check whether trade creditors figures is excluded to ascertain paid stock.

(xvi) To check whether unpaid LC bills or LC on documents against acceptance (DA) terms stock excluded while computing DP.

(xvii) To check whether Bank Hypothecation Board prominently displayed.

Credit Audit

6.11 Credit audit examines compliance with extant sanction and post sanction processes / procedures laid down by the bank from time to time. This audit is conducted:

(i) To verify whether loans and advance have been sanctioned properly (scrutiny at appropriate level).

(ii) To verify whether credit limits are reviewed or not.

(iii) To verify the security documents(both for Primary and collateral) held with the banks *vis-a-vis* compliance of stipulation in the sanction letter.

(iv) To verify whether the documents are being executed before release of the loan.

(v) To verify whether the advance is being followed up and supervised regularly and whether QMS statements are being received and scrutinized by branch.

(vi) To verify whether the advance have been classified as per RBI guidelines.

(vii) To verify whether credit rating has been done as per the applicable RBI guidelines.

(viii) To verify whether charge duly created and CHG 1 appropriately filled up and filed within specified time with Registrar of companies in applicable cases.

6.12 Main objectives of the credit audit are, normally as under:

(i) Improvement in the quality of the credit portfolio of Bank.

(ii) Review of sanction process and compliance status of loans.

(iii) Feedback on regulatory compliance.

(iv) Independent review of credit risk assessment.

(v) Pick up early warning signals at the early stage of loan period, i.e., immediately after loan disbursement/fixation of credit limits and suggest remedial measures.

(vi) Recommend corrective action to improve credit quality, credit administration and credit skills of employees.

Risk Based Internal Audit

6.13 Banks have gradually moved towards risk-based internal audit which includes, in addition to selective transaction testing, an evaluation of the risk management systems and control procedures prevailing in various areas of a bank's operations. The implementation of risk-based internal audit means that greater emphasis is placed on the internal auditor's role in mitigating risks. While focusing on effective risk management and controls, in addition to appropriate transaction testing, the risk-based internal audit would not only offer suggestions for mitigating current risks but also anticipate areas of potential risks and play an important role in protecting the bank from various risks.

6.14 The precise scope of the risk based internal audit must be determined by each bank for low, medium, high, very high and extremely high risk areas. It should review/ report on:

(i) Process by which risks are identified and managed in various areas.

(ii) The control environment in various areas.

(iii) Gaps, if any, in control mechanism which might lead to frauds, identification of fraud prone areas

(iv) Data integrity, reliability and integrity of MIS.

(v) Internal, regulatory and statutory compliance.

(vi) Budgetary control and performance reviews.

(vii) Transaction testing/ verification of assets to the extent considered necessary.

(viii) Monitoring compliance with the risk based internal audit report.

6.15 RBI has advised banks to adopt a framework for Risk-based Internal Audit to ensure that the audit is undertaken in the bank in a risk focused manner. This would also facilitate in adoption of the Risk-based Supervision framework. In this regard, RBI has issued circular RBI/2015-16/352DBS.CO.PPD.10887/11.01.005/2015-16dated March 31, 2016 on "Risk Based Supervision – Follow up of Risk Management Systems in Banks".

6.16 Further, "Master Circular on Audit Systems" dated September 26, 2012 issued by the Department of Financial Services, Government of India, inter alia lays down the following "Guiding Principles on Risk Based Internal Audit (RBIA)":

(i) RBI team should also carry out IS compliance audit as part of their audit routine for small & low rated branches as well as follow up work for non-compliance issues of the branch in IS audit areas.

(ii) Conflict of interest between audit team member and audited should be avoided.

(iii) The frequency of audits under Risk based system should be uniformly fixed at 9-12 months for extremely high/ high risk branches and 15-18 months for low risk branches.

(iv) Risk assessment matrix for branches/ departments given in the manual under the suggested RBIA policy may be adopted by banks.

(v) Audit team should guide the branches on spot rectification of the deficiencies to the extent possible.

(vi) It is advised that all the audit qualifications should be rectified within 90 days of submission of audit report and to be closed not later than 120 days.

Information Systems (IS) Audit

6.17 Setting up of a secure Information System goes beyond mere computerization of manual process. The system should safeguard its assets and maintain data integrity. It should help in achieving the organization's goals. A secure information system is expected to have established comprehensive procedures and controls, which are backed by commitment from the management. It is required to periodically monitor that these procedures and controls are in place and operational to effectively ensure that the information stored in these systems continues to be dependable. Periodical monitoring is achieved by Information Systems (IS). IS audit is a process of collecting and evaluating evidence/information to determine whether a computer system could:

(i) safeguard its assets (hardware, software and data) through adoption of adequate security control measures;

(ii) maintain data integrity;

(iii) achieve goals of the organization effectively; and

(iv) result in the efficient use of the available Information System resources.

6.18 IS audit assumes greater importance in the context of the accelerated pace of computerization taking place in the banking and financial sector in the country. Uncontrolled use of computers can cause loss of important data. Inaccurate or untimely data can lead to incorrect decision making. Computer frauds, caused by outsiders or insiders, can land the banking and financial organisations in serious trouble. The absence of adequate security controls and necessary perpetual vigilant mechanism would render the detection of computer frauds a matter of chance only. Computer error can prove costly in the long run and loss of confidential data or loss of confidentiality of data can lead to loss of reputation and legal wrangles.

RBI vide it's circular "Information System Audit – A review of Policies and Practices" dated April 30, 2004 has advised banks to carry out a systems audit periodically to assess the effectiveness of the hardware, software and operations to identify any changes required therein based on the said guidelines.

6.19 Further, "Master Circular on Audit Systems" dated September 26, 2012 issued by the Department of Financial Services, Government of India, inter alia lays down the following "Guiding Principles on Information Systems (IS) Audit":

(i) Banks should form separate IS Audit teams with persons having adequate IT experience and suitably CISA qualified professionals. The IS Audit should be carried out on a continuous adopting Risk based approach as per the IS Audit policy.

(ii) Continuous IS Audit should be introduced in critical areas in a phased manner.

(iii) Assessment of Internal Audit resource involvement at appropriate levels should be done.

(iv) IS Audit should become essential part of Internal Audit in the post CBS scenario.

(v) Branch managers should submit compliance of Do's and Don't's regarding IS Audit Key areas, on monthly basis.

Forensic Audit

6.20 The concept of Forensic audit may be defined as "A concentrated audit of all the transactions of the entity to find the correctness of such transactions and to report whether or not any financial benefit has been attained by way of presenting unreal picture. This audit aims at legal determination whether fraud has actually been occurred or not. It also aims the naming of person involved. Thus forensic audit involves examination of legalities by blending the techniques of propriety audit, regulatory audit, investigative audit and financial audit. The objective is to find out whether or not true business value has been reflected in the financial statement and in the course of examination to find whether any fraud has taken place.

6.21 RBI Master Circular on "Frauds - Classification and Reporting" dated July 1, 2015*inter alia* lays down certain requirements with regard to forensic audit in case of banks. Further, computer forensics is part of forensic audit and involves use of various tools to gather or collect data, examine the data, analysing the data and followed by reporting the finding. Data mining techniques are also used as a forensic audit technique which involves use of computer assisted audit techniques to mine large volumes of data for new, hidden or unexpected information or patterns.

PART II

Domain of Concurrent Audit

Chapter 1

Evolution and General Guidelines of Concurrent Audit

Introduction

1.1 Though a system of concurrent audit was already in existence in large and exceptionally large bank branches, it was formally introduced by the Reserve Bank of India *vide* its circular of October 1993. This measure of the Reserve Bank of India (RBI) arose out of the recommendations of the *Ghosh Committee on frauds and Malpractices in Banks*. In its said circular, the banking regulator explained concurrent audit as being "an examination which is contemporaneous with the occurrence of transactions or is carried out as near thereto as possible. It attempts to shorten the interval between a transaction and its examination by an independent person." The primary objective of the introduction of a formal system of concurrent audits in banks was to serve as an administrative support to branches. The RBI circular also clarified that concurrent audit is essentially a management process. The importance of concurrent audit was highlighted by the banking regulator as being essential for:

- Sound internal accounting functions.
- Effective controls.
- Setting the tone for vigilance internal audit to preclude incidence of serious errors and fraudulent manipulations.

1.2 Subsequently, a working group was set up by RBI under the Chairmanship of Shri Jilani, (the then Chairman, Punjab National Bank) to review internal control, inspection and audit system in banks.

Further, some of the Public Sector Banks had also sought additional guidelines on the scope of the system, coverage, reporting procedures, remuneration payable to concurrent auditor, etc. Accordingly, RBI, in consultation with Audit Sub-Committee of the Board for Financial Supervision, revised the guidelines vide its circular dated 14thAugust, 1996.

RBI issued another circular on12thAugust, 1997 in connection with Concurrent Audit System –Foreign Exchange Transactions - Enlargement of scope.

1.3 The RBI in its circular "*Concurrent Audit System in Commercial Banks – Revision of RBI's Guidelines*" issued in the month of July 2015 felt that in view of the changes in banks' organizational structure, business models, use of technology (implementation of Core Banking Solution), etc., a need is felt to have are-look at the concurrent audit system in the banking sector.

Since the concurrent audit system is regarded as part of a bank's early warning system to ensure timely detection of irregularities and lapses, which also helps in preventing fraudulent transactions at branches, the bank's management may continue to bestow serious attention to the implementation of various aspects of the system such as selection of branches/coverage of business operations, appointment of auditors, appropriate reporting procedures, follow-up/rectification processes and utilization of the feedback from the system for appropriate and quick management decisions.

1.4 The above-mentioned RBI Circular on concurrent audit specifies the following with respect to appointment of auditors and accountability:

(i) The option to consider whether concurrent audit should be done by bank's own staff or external auditors(which may include retired staff of its own bank) is left to the discretion of individual banks.

(ii) Appointment of an external audit firm may be initially for one year and extended upto three years, after which an auditor could be shifted to another branch subject to satisfactory performance.

(iii) If external firms are appointed and any serious acts of omission or commission are noticed in their working, their appointments may be cancelled and the fact may be reported to RBI & ICAI.

1.5 The aforesaid RBI circular lays down that it has been represented that concurrent audit is not often effective because adequate facilities in terms of space, availability of records, etc. are not available. To improve the effectiveness of concurrent audit, it is suggested that:

(i) banks arrange for an initial and periodical familiarization process both for the bank's own staff when entrusted with the concurrent audit and for the auditors appointed for the purpose.

(ii) all relevant internal guidelines/circulars/important references as well as relevant circulars issued by RBI/SEBI and other regulating bodies should be made available to the concurrent auditors on an on-going basis.

(iii) Regular and timely submission of audit data including system generated reports is a key for the success of Concurrent Audit in Banks

Scope of Concurrent Audit

1.6 Scope of concurrent audit as defined in the RBI Circular is as follows:

(i) The Concurrent audit is an examination which is contemporaneous with the occurrence of transactions or is carried out as near thereto as possible. It attempts to shorten the interval between a transaction and its examination by an independent person. There is an emphasis in favour of substantive checking in key areas rather than test checking.

(ii) This audit is essentially a management process integral to the establishment of sound internal accounting functions and effective controls and setting the tone for a vigilant internal audit to preclude the incidence of serious errors and fraudulent manipulations.

(iii) A concurrent auditor may not sit in judgment of the decisions taken by a branch manager or an authorized official. This is beyond the scope of concurrent audit. However, the audit will necessarily have to see whether the transactions or decisions are within the policy parameters laid down by the Head Office, they do not violate the instructions or policy prescriptions of the RBI, and that they are within the delegated authority.

(iv) In very large branches, which have different divisions dealing with specific activities, concurrent audit is a means to the in-charge of the branch to ensure on an ongoing basis that the different divisions function within laid down parameters and procedures.

Coverage of Business/ Branches

1.7 In view of significant developments in the banking sector during the past decade, it is required that new areas posing risk may be brought under the purview of concurrent audit. A large number of activities/ operations are being carried out in a centralized manner at various units set up for that purpose and the scale of transactions/ operations undertaken at these units is large. With a view to ensuring that the functioning of these units is as per the internal as well as regulatory guidelines and mitigating the risk associated with large-scale operations, such non-branch units may be brought under the purview of concurrent audit.

While selecting the branches for concurrent audit:

(i) The risk profile of the branches needs to be considered. The branches with high risk are to be subjected to concurrent audit irrespective of their business size.

(ii) Further, all specialized branches *viz*.,

- Agri, SME,
- Corporate,
- Retail Assets,
- Portfolio Management,
- Treasury, Forex, Back Office, etc.,

may be covered under concurrent audit. Certain areas where risk has reduced on account of computerization, implementation of core banking system may be excluded from the purview of concurrent audit.

1.8 The following branches, business activities/verticals of a bank may be subject to concurrent audit:

(i) Branches rated as high risk or above in the last Risk Based Internal Audit (RBIA) or serious deficiencies found in Internal Audit.

(ii) All specialized branches like, Large Corporate, Mid Corporate, exceptionally large/very large branches (ELBs/VLBs), SME.

(iii) All Centralized Processing Units like:

- Loan Processing Units (LPUs),

- Service branches,
- Centralized account opening divisions, etc.

(iv) Any specialized activities such as wealth management, portfolio management services, Card Products Division, etc.

(v) Data Centers.

(vi) Treasury/branches handling foreign exchange business,

(vii) Investment banking,

(viii) Bigger overseas branches.

(ix) Critical Head Office Departments.

(x) Any other branches or departments where, in the opinion of the bank, concurrent audit is desirable.

(xi) Concurrent audit at branches should cover at least 50% of the advances and 50% of deposits of a bank.

Types of Activities to be Covered

1.9 Revised RBI circular on concurrent audit specifies following types of activities to be covered under concurrent audit:

(i) The main role of concurrent audit is to supplement the efforts of the bank in carrying out simultaneous internal check of the transactions and other verifications and compliance with the procedures laid down.

(ii) The scope of concurrent audit should be wide enough/focused to cover certain fraud - prone areas, such as, handling of cash, deposits, advances, foreign exchange business, off-balance sheet items, credit-card business, internet banking, etc.

(iii) The detailed scope of the concurrent audit should be clearly and uniformly determined for the bank as a whole by the bank's Inspection and Audit Department in consultation with the bank's Audit Committee of the Board of Directors (ACB).

(iv) In determining the scope, importance should be given to checking high-risk transactions having large financial implications as opposed to transactions involving small amounts.

(v) While the detailed scope of concurrent audit may be determined and approved by ACB. Besides, the items where RBI has specifically advised the banks to be covered under concurrent audit, may also be part of the checklist of the concurrent auditor.

Preparation of Audit Programme

1.10 The concurrent auditor should also prepare a formal concurrent audit programme listing the procedures essential for meeting the objective of the concurrent audit plan. Though the form and content of the audit programme and the extent of its details would vary with the circumstances of each case, yet the concurrent audit programme should be so designed as to achieve the objectives of the engagement and also provide assurance that the concurrent audit is carried out in accordance with the Standards on Internal Audit issued by institute of Chartered Accountants of India.

1.11 The concurrent audit programme identifies, in appropriate details, the objectives of the concurrent audit in respect of each area, the procedures to be performed to achieve those objectives, the staff responsible for carrying out the particular activity, the time allocated to each activity as also the sufficiently detailed instruction to the staff as to how to carry out those procedures. The concurrent audit programme may also have provision for information, such as, the procedures actually performed, reasons for not performing the originally identified procedures, actual time consumed in carrying out the relevant procedure, reasons for deviations from budgeted time, etc. A well-prepared, comprehensive audit programme helps proper execution of the work as well as of the proper supervision, direction and control of the performance of the engagement team.

Audit Planning and Documentation

1.12 The concurrent auditor should document matters which are important in providing evidence that the concurrent audit was carried out in accordance with the basic principles of an audit and as per terms of reference. The Institute has also issued Standard on Internal Audit (SIA) 3, *Documentation*. This should also be referred for the purpose.

1.13 The concurrent auditor should record the audit plan as per the checklist and the format of audit report given by the respective bank's circulars, terms of engagement, scope of work, etc., and the engagement letter should also be taken into consideration in this regard.

1.14 The concurrent auditor should keep all the working papers on record which are used in finalizing the reports. The following papers can be kept in permanent audit file:

- Letter of engagement, undertaking/comment by the firm to the bank.
- Audit checklist.
- Information regarding branch business, data, nodal officer, status of branch, whether computerized/parallel category of branch, etc.
- Performance of monthly, quarterly, annual report revenue report.
- Correspondence with the bank for any matter.

1.15 Similarly, the current audit file may include all other papers relevant to the concurrent audit, for example:

- Branch Audit Programme.
- Branch's statement as on the data of the report on which basis it is prepared.
- Periodic correspondence with the concerned departmental officer.
- Irregularities intimated to the Controlling Officer.
- Discussion of the audit report.
- Particulars of big borrowers, depositors, etc.
- Circulars received from head office of the audited bank.

It is necessary for the auditor to record his observation in an appropriate record and bring them to the notice of concerned official of the Bank.

Relative Importance to Different Areas

1.16 The purpose of concurrent audit is substantive checking in key areas with the appropriate design of audit sampling. The concurrent auditor, normally, goes through the vouchers and other books of the branch of the previous day and identifies areas to be scrutinized in details. In case the volume of transaction and deposit/advances at the branch are heavy and it is not possible to conduct 100 percent checking the next day, the concurrent auditor may concentrate on high value transactions having material financial implications for the Bank rather than those involving lesser amount but having no material financial impact on the bank.

In any case, the examination of all transactions as per prescribed norms should be done. Generally, the following guidelines may be followed:

- The concurrent auditor would examine the workings of each department and identify problem areas and loopholes.
- The concurrent auditor would observe that necessary compliance of the prescribed systems and procedures is done in the branch.
- The concurrent auditor should indicate the extent of checking of various areas in his report. If the same is not given in the format in which the report is to be submitted, reference of this fact may be made in covering letter of the report.

Frequency of Checking Different Items

1.17 The frequency of checking of different items by the concurrent auditor depend on factors, such as, the guidelines given by the bank in the scope of work, circulars issued by the RBI from time to time, etc. A concurrent auditor needs to devise his own strategy/timeframe covering all the areas. For this purpose, the auditor would need to first identify the areas at the branch which need greater attention, the areas which are to be regularly monitored, the items which are to be checked daily, and the items which may be checked less frequently.

1.18 The concurrent auditor would also need to go through the previous reports such as, the statutory audit report, internal inspection reports, RBI inspection reports, stock audit report and concurrent audit reports of the branch as well for this purpose. Illustrative checklist is given in Part III of this Manual.

Focus of Concurrent Audit

1.19 A study of the *modus operandi* of the fraudulent transactions, generally, indicates that the processing of transactions is done without adhering to the systems and procedures. This permits an unscrupulous person to misuse the procedures of the bank and undertake fraudulent transactions, which remains unnoticed for a long time. Concurrent Auditor would therefore, need to focus on adherence to laid down systems and procedures and safe guards.The Auditor needs to conduct this independent assessment of audit risk *vis-a-vis* the internal control in the branch while finalizing the audit programme.

Maintenance of Appropriate Record

1.20 In order to keep correspondence between the branch in charge and the concurrent auditor under control, instead of daily/weekly reports, the concurrent auditor may maintain a record of his observations, duly countersigned by the bank official in the earliest possible period. The recording should be made on a daily basis with date with suitable column for recording rectification/removal. The record preferably remains in the custody of the incumbent in-charge with a copy to concurrent auditor.

Various items to be, normally, recorded are given below:

Date	Irregularity Observed	Initial/authorization of Concurrent Auditor	Initial of Bank Official

How Irregularity Was Rectified	Date of Rectification	Initial/ Authorization of Concurrent Auditor	Initial of Bank Official

1.21 The record should be made available to the officer in charge of the controlling office or their representatives as and when they visit the branch to apprise them of the state of working of the branch, removal/rectification of irregularities by the branch, compliance of systems and procedures by the branch.

Reporting System

1.22 The bank may devise a reporting system and periodicity of various check list items as perits sensitivity. Minor irregularities pointed out by the concurrent auditors are to be rectified on the spot. Serious irregularities should be straightaway reported to the Controlling Offices/Head Offices for immediate action.

Whenever fraudulent transactions are detected, they should immediately be reported to Inspection and Audit Department (Head Office) as also to the Chief Vigilance Officer as well as Branch Managers concerned (unless the branch manager is involved).A special report may be submitted by the concurrent auditor in situations of any serious irregularity/ frauds, etc. In such cases, the concurrent auditor should get in touch with the higher authorities at the earliest besides sending a special report/flash report to the higher authorities, explaining the findings of the case.

The issue needs to be discussed with the Branch manager and his feedback/ views to be mentioned in his special report.

1.23 There should be proper reporting of the findings of the concurrent auditors. For this purpose, each bank should prepare a structured format. The major deficiencies/aberrations noticed during concurrent audit should be highlighted in a special note and given immediately to the bank's branch controlling offices. A quarterly review containing important features brought out during concurrent audits should be placed before the ACB.

Follow-up action on the concurrent audit reports should be given high priority by the Controlling Office/Inspection and Audit Department and rectification of the features done without any loss of time.

Removal of Irregularities

1.24 To supplement the process of removal/rectification of irregularities in the earliest possible period, the concurrent auditor will bring his finding of the irregularities/ deficiencies/discrepancies to the notice of the branch officials. The outstanding deficiencies/irregularities need to be discussed with branch officials and their viewpoints also need to be reflected. The concurrent auditor should maintain an appropriate record of the irregularities observed as well as the discussions held with the branch officials. Pending irregularities not rectified would be included in the final report of the concurrent auditor. Materiality of the spending irregularities should be clearly spelt out in the final report. The Controlling Officer's view on these final queries should also be noted down.

1.25 The irregularities pointed out in the previous monthly/quarterly concurrent audit reports may be dropped by the concurrent auditor with proper disclosure if the same have been rectified.

The concurrent auditor should get the guidelines implemented in respect of following sensitive areas on priority basis to avoid the occurrence of these irregularities:

- Morning checking, i.e., checking of all computers generated supplementary, checksum generation checking, previous day's G.L. Day Book, Exceptional Transaction Report, Day beginning by System Administrator as per Computer Manual, etc.
- Teller's reconciliation.
- Custody, checking and use of scrutiny forms.
- Safekeeping of AOF's, ledgers, teller cards, etc.
- Use of password by the password holder himself and initialling each entry in Audit Trail/Transactions list by, the password holder, and the same appears in the printout.
- Post sanction and periodic verification of securities.
- Correct provisioning of interest on deposits and advances and proper maintenance of the Interest Register.

1.26 Certain irregularities, like, excess cash, suspense entries, defects in AOF checking, bills, insurances, etc., find place in many of the reports. Cash Ratio limit in terms of percentage and/or amount is fixed by the higher authorities. Variations, if any, should be reported by the concurrent auditor.

The concurrent auditor should, however, permit a reasonable time for the completion of the formalities. In case the branch officials do not co-operate in rectification of the irregularities, the concurrent auditor may contact/write to the higher authorities.

Minimum Audit Programme for Concurrent Audit

1.27 Minimum Audit Programme for Concurrent Audit has been prescribed in RBI Circular "Concurrent Audit System in Commercial Banks – Revision of RBI's Guidelines" dated July 16, 2015, which is as follows:

A. Cash transactions –Verify

(i) Surprise physical verification of cash at branch and ATM along with safekeeping and custody.

(ii) Daily cash transactions, particularly any abnormal receipts and payments.

(iii) Surprise verification of cash by an officer other than the joint custodian.

(iv) Proper accounting of and availability of insurance cover for inward and outward cash remittances.

(v) Accounting of currency chest transactions and delays/omission in reporting to RBI.

(vi) Reporting of Counterfeit Currency.

(vii) All cash transactions of Rs. 10 lakh and above reported in CTR.

(viii) That all cash transaction of Rs. 50,000 and above invariably indicate Pan No./Form 60.

B. Clearing transactions –Verify

(i) Reconciliation with bank's account at Clearing House and review of old outstanding entries for reconciliation.

(ii) Drawings allowed against uncleared instruments - sanction by the controlling authority.

C. Remittances/Bills for Collection –Verify

(i) Remittance of funds by way of DDs/TTs/MTs/TC/NEFT/RTGS any other mode in cash exceeding the prescribed limit.

(ii) Documents of title (lorry receipts, railway receipts, etc.) obtained in favour of the bank and the concerned transporters are on the IBA approved list.

(iii) Outstanding balance in DP and other transit accounts pending payment beyond prescribed period.

D. Deposits –Verify

(i) Adherence to KYC/AML guidelines in opening of fresh accounts and monitoring of transactions in such accounts.

(ii) Large term deposits received and repaid including checking of repayment of term deposit in cash beyond permissible limit.

(iii) Accounts opened and closed within a short span of time i.e., accounts with quick mortality.

(iv) Activation and operations in inoperative accounts.

(v) Value dated transactions.

(vi) Settlement of claims of deceased customers and payment of TDRs against lost receipts and obtention of indemnities, etc. To check revival of dormant accounts and accounts with minimum activities.

(vii) Examination of multiple credits to single accounts.

E. Treasury operations –Verify

(i) If branch has acted within HO instructions for purchase and sale of securities.

(ii) Periodic confirmation of Derivative contracts with counterparties.

(iii) Adherence to regulatory guidelines with respect to Treasury deals/structured deals.

(iv) Controls around deal modification/cancellation/deletion, wherever applicable.

(v) Cancellation of forward contracts and passing/recovery of exchange gain/loss.

(vi) Gaps and OPL maintained in different currencies vis-à-vis prescribed limit for the same.

(vii) Reconciliation of Nostro and Vostro accounts balances in Nostro accounts in different foreign currencies are within the limits prescribed by the bank.

(viii) Collection of underlying documents for Derivative & Forward contracts. Delays, if any.

(ix) Instances of booking and cancellation of forward contracts with the same counter party within a span of couple of days or a few days.

(x) Sample check some of the deals and comment on the correctness of computation.

(xi) Checking of application money, reconciliation of SGL account, compliance to RBI norms.

(xii) Checking of custody of unused BR Forms and their utilization in terms of Master Circular on Prudential Norms on Classification, Valuation and Operations of Investment Portfolio by banks.

(xiii) To ensure that the treasury operations of the bank have been conducted in accordance with the instructions issued by the RBI from time to time.

F. Loans & Advances-Verify

(i) Report Bills/cheques purchased, if in the nature of accommodation bills.

(ii) Proper follow-up of overdue bills purchased/discounted/ negotiated.

(iii) Fresh loans and advances (including staff advances) have been sanctioned properly and in accordance with delegated authority.

(iv) Reporting of instances of exceeding delegated powers to controlling/head office by the branch and have been confirmed or ratified by the competent authority.

(v) Securities and documents have been received as applicable to particular loan.

(vi) Securities have been properly charged/ registered and valued by competent person. Whether the same has been entered in the bank's system.

(vii) All conditions of sanction have been complied with.

(viii) Master data relating to limit, rate of interest, EMI, moratorium period details have been correctly entered and updated/modified in the system.

(ix) Value dated entries passed in advances accounts.

(x) Post disbursement supervision and follow-up is proper, such as timely receipt of stock and book debt statements, QIS data, analysis of financial data submitted by borrower, verification of securities by third parties, renewal of limits, insurance, etc.

(xi) Whether there is any misutilisation of the loans and whether there are instances indicative of diversion of funds.

(xii) Compliance of prudential norms on income recognition, asset classification and provisioning pertaining to advances.

(xiii) Whether monthly updating of drawing power in the computer system on the basis of stock statements/book debt statement/ other financial data received from the borrowers.

(xiv) Recovery in compromise cases is in accordance with the terms and conditions of the compromise agreement.

(xv) To check review and renewal of loans.

G. LC/BG –Verify

(i) LC/BG issued/amended as per the approved format/model guarantee prescribed and standard limitation clause incorporated. Whether counter indemnity obtained as prescribed.

(ii) Any deviation from the terms of sanction in regard to margin, security, purpose, period, beneficiary, collection of charges, commission/fee, etc.

(iii) Whether payment is made to the debit of party's account on due date without creating overdraft/debiting suspense, in case of deferred payment guarantee.

H. Foreign Exchange Transactions-Verify

(i) Recovery of charges as per HO Guidelines.

(ii) Packing credit released, whether backed by LC or confirmed export order.

(iii) Availability of ECGC cover and compliance with ECGC terms.

(iv) Submission of statutory returns on export/ import transactions, like BEF statements, XOS, write off of export bills, etc. Follow up of outstanding export bills and exchange control copy of bill of entry.

(v) Irregularities in opening of new accounts and operation in NRO, FCNR, NRE, EEFC, etc., and debits/credits entries permissible under the rules.

(vi) Whether operations in FCRA accounts are as permitted by MHA and FCRA guidelines.

(vii) Booking, utilization, extension and cancellation of forward contracts.

I. House Keeping –Verify

(i) Exceptional transaction reports are generated and verified by branch staff as prescribed.

(ii) Review of all balance sheet heads and outstanding entries in accounts, e.g., suspense, sundry and inter-bank accounts. Review of follow up of entries pending for reversal.

(iii) Scrutiny of daily vouchers with more emphasis on high value transaction including high value expenses and debit entries in Suspense account.

(iv) Debits in accounts where signatures are pending for scanning.

(v) Whether records related to KYC/vouchers and other critical areas are sent to specific places like archival centre, record room as per stipulated periodicity.

(v) Adherence to KYC/AML guidelines in opening fresh account and subsequent modifications of records and monitoring of transaction.

J. Verification of Merchant Banking Business-Verify

(i) Whether the instructions given by the controlling branch are properly followed where the branch acts as a collecting branch for issue business.

(ii) Whether daily collection position is advised to the controlling branch.

(iii) Whether recovery of the commission/fees and out of pocket expenses as agreed with the respective companies and whether the competent authority has duly authorized any waiver or reduction of such charges.

(iv) Whether the prescribed preventive vigilance measures are observed by the branch.

(v) Where data entry or data processing work is entrusted to outside agencies, the competent authority duly approves these and the prescribed stamped indemnity has been obtained from such agencies.

(vi) Whether dividend interest warrants/refund payment accounts of companies are funded prior to dispatch of the relative warrants by the companies and there is no misuse of the facility.

(vii) Whether Claims for reimbursement of amounts of paid warrants received from paying branches are processed and debited to the concerned company's account promptly.

(viii) Whether charge on security has been created, wherever debenture trustee activity is undertaken by bank.

K. Verification of Credit Card/Debit card –Verify

(i) Application for the issue of credit card has been properly examined and record of issue of the same has been maintained.

(ii) Whether overdraft/debits arising out of the use of credit cards are promptly recovered and informed to higher authorities.

(iii) Whether undelivered credit cards are properly kept as security items and followed up with credit card department for further instructions.

(iv) Physical verification of ATM cards, debit cards, credit cards, passwords and PINS, control over issue & delivery, safe keeping and custody at all the locations. Report loss of any such items.

L. Others –Verify

(i) Compliance of provisions relating to Tax Deducted at Source, service tax, trade tax, other duties and taxes.

(ii) Physical verification of inventory, control over issue of inventory, safe keeping and custody of security forms. Report any loss of such items.

(iii) Physical verification of other deliverable items, control over issue, safe keeping and custody.

(iv) Physical verification of Gold coins, control over issue, safe keeping and custody. Checking of Gold sale transactions.

(v) Custody and movement of branch keys.

(vi) Locker keys and locker operations-linking of FDR as security for locker/operation of locker/inoperative lockers/ nomination/other issues.

(vii) Safe custody of branch documents like death claim cases, issuance of duplicate DD/PO/FDR, checking of indemnities, etc. and verification of documents executed during the period under audit.

(viii) Reporting of frauds.

Chapter 2
Concurrent Audit Universe

2.1 The concurrent auditor may scrutinize certain daily transaction of the branch, as per terms of the Bank and in absence of any specific guidelines, on the same day and certain others on the next working day. He may scrutinize certain items at periodical intervals and other lesser important items on any day of the month maintaining random sampling and surprise element. The concurrent auditor is, normally, required to carry out audit of transaction on the basis of daily vouchers, general ledger balance book, subsidiary books, and ledgers.

2.2 To facilitate the work of a concurrent auditor and ensure that he/they doesn't miss any important aspect, the checklist for audit is prepared according to the size of the branch by the auditor himself in accordance with the guidelines and instructions of the particular Bank. This checklist is however, normally, given by each Bank and is to be followed by the Concurrent Auditor. For preparing this checklist, one of the approaches followed is to prepare it on the basis of items to be verified on daily basis, weekly basis, fortnightly basis, monthly basis, quarterly basis, half yearly basis and yearly basis. The various items of banking transaction/services to be verified are enumerated in the subsequent paragraphs.

Deposits

2.3 The main source of bank finance is the deposits accepted from public. To cater to the needs of various types of customers, banks offer different types of accounts with various facilities attached to these accounts. The Bank accounts are broadly classified into the following categories:

(i) Savings Deposit;

(ii) Current Deposit;

(iii) Fixed Deposit;

(iv) Recurring Deposit;

(v) Saving cum fixed deposit/Swift A/C;

(vi) Non-resident Account; etc

Savings Deposit Account

2.4 The Savings Deposit Accounts are opened to attract small savings of the public. The number of withdrawals per year is, normally, restricted. A Savings Deposit cannot be opened by any trading or business concern, whether it may be individual, or partnership concern, etc. A bank may open savings deposit account for the primary cooperative credit society which is financed by that Bank, companies incorporated under Section 25of the Companies Act, 1956; cooperative societies, philanthropic associations and institutions which are exempt from payment of income-tax with the prior permission of the RBI. No overdraft is, normally, allowed on Savings Account, except Pradhan Mantri Jan-Dhan Yojana (PMJDY).

Fixed Deposit Account

2.5 Fixed Deposits, named differently by Banks, are the funds kept by the public with the Bank, which are not required immediately and are repayable on the expiry of term of the deposits. The period of deposits may vary from 7 days to 5 years or even more than 5 years. The rate of interest varies depending on the period the deposit is kept and certain other parameters as decided by the banks, like, Senior Citizens/ retired staff. However, the benefit shall not accrue to staff other than retired/ superannuated unless the bank specifically mentions. Sometimes large value deposits are given special rate of interest by the banks.

Classification of Deposits

2.6 For the purposes of the disclosures in the Balance Sheet, the RBI classifies the deposits accepted by Bank into following categories, namely:

I. Demand Deposits

II. Savings Bank Deposits

III. Term Deposits

I. Demand Deposits

(i) From Banks	Includes all Bank deposits repayable on demand.
(ii) From Others	Includes all demand deposits of the non-Bank sector. Credit balances in overdrafts, cash credit accounts, deposits payable at call, overdue deposits current accounts whether inoperative or not, matured term deposits, and cash certificates, certificates of deposits, etc. are to be included under this category.

II. Savings Bank Deposits

Includes all savings Bank deposits(including inoperative savings Bank accounts)

III. Term Deposits

(i) From Banks	Includes all types of Bank deposits repayable after a specified term.
(ii) From Others	Includes all types of deposits of the non-Bank sector repayable after a specified term. Fixed Deposits, cumulative and recurring deposits, cash certificates, certificates of deposits, annuity deposits, deposits mobilized under various Term based schemes, foreign currency non-resident deposit accounts, etc. are to be included under this category.

Notes:

Deposits included under demand deposits as per RBI classification are:

(i) Credit balance in overdrafts and Cash Credit accounts.

(ii) Deposits payable at call

(iii) Overdue deposits

(iv) Inoperative current accounts

(v) Matured term deposits and cash certificates

(vi) Certificates of deposits, etc.

2.7 The cash credit account would be included if the balance is showing credit balance. The current accounts are also payable on demand. The outstanding telegraphic and mail transfer demand drafts are also to be included under the demand deposit head.

2.8 Term deposits as per the classification would include:

(i) All deposits repayable after a specified term

(ii) Fixed deposits

(iii) Cumulative and recurring deposits

(iv) Cash certificates

(v) Certificates of deposits

(vi) Annuity deposits

(vii) Deposits mobilized under various schemes

(viii) Ordinary staff deposits

(ix) Foreign currency

(x) Non-resident deposit accounts, etc.

Advances

2.9 The lending of funds to customers is the main business of a banking company. A bank earns income from the interest and discount, etc. arising out of the funds lent by it. The lending of funds has inherent-risks, i.e. the loan or advance may go bad.

Banks, therefore, follow prudential lending principles as prescribe dy the Reserve Bank of India and Bank's internal policy guidelines while lending the funds in order to reduce the associated risks.

Various Forms of Credits

2.10 The advances made by banks are, normally, in the following forms:

(i) Cash Credit

(ii) Overdraft

(iii) Loans

Cash Credit

2.11 Cash credit, is an arrangement between a bank and the customer by which money is advanced against hypothecation of stocks in trade, book debts and a bond of credit by one or more sureties. The borrower can reduce the debit balance by paying back surplus available with him and redraw the amount as and when needed. The interest is charged on the amount utilized. In certain cases, commitment fee is charged for non-utilisation of arrangement as agreed.

2.12 Cash credit is, normally, sanctioned by the bank for a period of one year and is, generally, renewed if the account is operated satisfactorily. The cash credit is generally secured by tangible assets. The borrower need not withdraw the whole amount and may withdraw the funds as and when required. The maximum amount sanctioned depends on the working capital requirements of the borrower. The interest is charged monthly on the outstanding debit amount to the debit of the borrower's account.

Overdraft

2.13 The overdraft, unless the nomenclature is used by some Bank for certain type of withdrawals of secured/unsecured type, is a facility given by a bank to me temporary needs of the borrower. An overdraft facility is usually sanctioned against securities like shares, stock, bonds, Bank's own fixed deposit receipt, Govt. Securities, like, NSC, life insurance policy (surrender value), immovable property, etc.

Loan

2.14 A loan is a lump sum payment to the borrower. The borrower can withdraw the amount at once or keep it in his account and withdraw as per his needs. The repayment terms are settled in advance. A loan may be a demand loan or term loan. A demand loan is repayable over a fixed period. A loan which is repayable within 3 years is called a short term loan. Loans repayable within a period of 3 to 5 years are called medium term loans and loans repayable beyond 5 years are long term loans. Sometimes loans are disbursed over a period depending on the requirement of the borrower. The interest is charged on the amount disbursed as reduced by the repayment, if any, on daily outstanding balances. When the loan is disbursed in stages, the enduse is generally enquired into before the disbursement of subsequent instalments. The repaid amount is not allowed to be redrawn even if it is by way of prepayment

2.15 Loans can be either secured or unsecured. An *unsecured loan* is one for which the bank holds no security other than the personal guarantee of the borrower. Such loans are now an uncommon feature except personal loans. A bank also extends term loans for the purpose of purchase of assets. The repayment is fixed in advance by way of instalments. When only a part of the advance is covered by securities as at the date of balance sheet, that part should be classified as secured and the remaining amount be shown as unsecured. Banks do not advance amounts equal to the value of the security but keep appropriate margin to provide for a decline in the value of security. RBI also directs from time to time, specified margins to be kept against some particular type of securities like Shares/ items of essential use, etc.

2.16 A commercial bank's performance is evaluated mainly on the quality of its housekeeping and proper functioning of its large network of branches. Numerous transactions involving huge sum of money take place every day at bank branches. The accounts of everyday transactions of a branch are prepared and reconciled every day. Any mistake/wrong accounting leads to enormous representation of true state of affairs of the branch to its controlling/head office. Any mistake in paying interest to the depositors and or realizing interest from the borrower's leads to revenue leakage in the banking sector.

2.17 There have been rapid changes in the lending activity undertaken by banks, marked by:

(a) Deregulation of interest rate

(b) IRAC norms, i.e., Income Recognition and Asset Classification.

(c) Stricter Provisioning and Capital Adequacy norms

(d) Introduction of Risk based Management System

(e) Lending though Cash Flow System in addition to MPBF System(Maximum Permissible Bank Finance).

2.18 In today's banking, the role of a bank can be stated to be threefold asunder:

(i) To make a proper selection of borrower, who is worthy of bank's assistance, both in terms of commercial principle and as well as the national priority;

(ii) To ensure that funds lent are safe; and

(iii) To ensure that good and proper use of bank credit is made by the borrower, judging from two angles - first, bank credit is not pre-empted as a result of inefficient working capital management, speculative build-up of inventory and secondly, bank credit is not diverted for "unauthorized use".

2.19 Undue emphasis of safety of funds, is however, not desired by the banking sector nowadays, since, if the advance is misutilized, i.e., used for the purpose' other than the originally intended one, it attracts comments notwithstanding safety of the same. Safety of advance does not merely depend upon the availability of security of adequate value; it is also based upon continued viability of the enterprise, because, if the enterprise is weak, it is extremely doubtful whether the security would fetch the value originally ascribed to it.

2.20 It is quite clear from the foregoing that concept of safety of funds in banks has changed, as it should, because no longer the banker does perform the role of a money-lender, but finances an economic activity and thus security is simply not synonymous with safety.

2.21 While discharging the duties of professional assignments entrusted by the banks, the concurrent auditor should, look into the aspect of supervision and follow-up of bank credit in order to protect the interests of the Bank. The broad aspects which maybe looked into are enumerated below:

(i) To see compliance with the terms and conditions of the sanction (essence of credit audit to be taken into consideration).

(ii) To undertake physical inspection of godown/factory, only if specifically desired by the Bank.

(iii) To observe continued viability of operations.

(iv) To verify the end use of bank credit.

Financial Follow Up

2.23 The financial follow-up devised by Chore Committee is an off shoot of RBI's concern on lack of proper follow-up procedures then prevalent in commercial banks. For such financial follow up the Chore Committee suggested certain Quarterly Information System to be provided by the borrowers to enable the bank to verify as to whether borrower's operating performance and finance management conform to the budget and promise made to the bank while availing the bank credit. This has been replaced by QMR/HMR Statement.

2.24 The concurrent auditor, while discharging his duties, should have knowledge of such follow-up statements as well as how they should be scrutinized to protect the interests of the bank. It is mandatory under the RBI regulations for a limit above a specified amount but below the cut-off point has been left to the discretion of the banks.

2.25 Particulars of QMR/HMR (which are now in use) replacing QIS are given below:

Description	Periodicity	Date of Submission
QMR I replacing QIS II	Quarterly	Six weeks after the Close of the Quarter to which it relates.

HMR I replacing QIS III	Half Yearly	Two months from the commencement of the half year to which it relates.

Credit Cards

2.26 The credit card operations occupy a special place in the modern day banking industry. A credit card has three important functions:

- It is an instrument of paying for goods and services
- It is an instrument of obtaining cash
- It is a source of revolving credit. Usually, there is a contract between the card issuer (the Bank) and the card holder(customer) whereby – the card holder is permitted to make use of the card at specified retail outlets (know as member establishments) to pay for the goods and services.

2.27 The mechanism of a credit card can be illustrated as follows:

As soon as the card holder makes purchases from specified retail outlets/member establishment, the retail outlets makes out bills to the account of the card holder and obtains payment from card organizations like Visa or Master immediately who in turn makes a bill to the Bank which issued the card. The Bank makes payments to Visa or Master immediately. Subsequently, the payment is realized from the respective card holder RuPay Card has been introduced in 2015 as an economic option and is being used, particularly, for Pradhan Mantri Jan-Dhan Yojana (PMJDY) scheme although not restricted for the scheme.

RBI has issued Master Circular DBR.No.FSD.BC.18/24.01.009/2015-16 on Credit Card, Debit Card and Rupee Denominated Co-branded Pre-paid Card Operations of Banks and Credit Card issuing NBFCs on July 1, 2015.

Types of Cards

2.28 There are many types of cards in the Indian market and the more popular ones are listed below:

Credit Card

It is an instrument of payment which enables the cardholder to obtain either goods or services from merchants where arrangements are made to reimburse the merchant. The outstanding amount is payable by the card holder to the bank over a specified period which carries specified rate of interest also.

Debit Card

It is a payment card used to obtain cash, goods and services by automatically debiting the payments to the cardholder's Bank account immediately. For this, the card holder must have credit balance in accounts whereto card pertains.

Co-branded cards

Co-branded cards are those that a bank promotes jointly with other non-financial institutions. Card holders use their cobranded cards in the same way as they use any other cards but each time they make a purchase, they accumulate points which enable them to claim discount in the price.

Frauds in Card Transaction

2.29 Wrongful use of lost and stolen card is the biggest area of fraud. Credit cards are sometimes picked up by unscrupulous persons and they use the cards indiscriminately before steps can be taken to hot list the cards by the issuing banks. Now, bank shave started issuing photo cards. Photo cards are useful as a marketing tool because people like having their picture on the card and it also serves to prevent fraud by impersonation of the cardholder.

Foreign Exchange Transactions

2.30 Branches dealing in foreign exchange are classified in three categories, The "A" categories are allowed to open and maintain currency-wise account with foreign banks/correspondents. These accounts are called Nostro accounts. While "B" category branches operate directly upon the account (Nostro accounts)opened by "A" category branches. The "C" category branches can handle foreign exchange business only through "A" and/or "B"class branches. The banks authorize some branches only to deal with spot or forward sale/purchase of foreign currencies with RBI, foreign correspondent banks, other banks in India. Foreign bank shave opened accounts with Indian banks for foreign exchange dealings. These accounts are called Vostro accounts.

2.31 All the foreign exchange business transactions are governed by the Foreign Exchange Management Act (FEMA),1999. A bank has to be very careful in dealing with foreign exchange transactions because it has to have full knowledge about foreign parties. The bank has to take care that the transaction does not violate the provisions of FEMA and the rules framed there under. The foreign exchange rate fluctuation is another hazard in these dealings and may involve loss.

2.32 The bank scrutinizes the documents, shipping bills and orders, etc. received from the customers and makes independent assessment of customers' standing and ability to meet the commitments. The banks enter into forward sale/purchase of foreign currency to protect their dealings in foreign exchange. The forward sale/purchase transactions would cover spot or forward purchase of foreign currencies.

2.33 The concurrent auditor has to look into the following factors involved in foreign exchange dealings of banks:

(i) Compliance with FEMA

(ii) Compliance with RBI rules.

(iii) Follow-up of procedures of authorized dealers.

(iv) Brokers' notes.

(v) Reconciliation/correspondent statements of Nostro accounts balances are to be reconciled with corresponding accounts.

(vi) Interest applicable on credit/debit balance on Nostro accounts and profit/loss on exchange accounts to be recorded in profit and loss account.

(vii) In the case of Nostro accounts, because the debits are raised later, on account of payments made of TTs/MTs/DDs drawn on Indian banks by foreign banks/exchange houses, etc. the interest loss can be avoided if the debts are value dated.

(viii) Overdrafts allowed in Nostro accounts.

(ix) Reconciliation of daily closing balances with accountholders and confirmations obtained.

(x) Maintenance of the Registers as per the requirements of RBI.

(xi) Submission of periodical returns to RBI.

2.34 The various statements to be filed by banks are as follows:

(i) Weekly return of various currencies held in different forms and monthly returns of bid bonds, guarantees issued, statement of non-resident accounts, export letters of credit, blocked accounts.

(ii) Fortnightly returns of export bills negotiated/sent for collection, outward remittances effected against imports sale/purchase transactions in foreign currencies.

(iii) The details regarding purpose, commodity, country, currency, terms of payment, etc.

(iv) Statement of overdue export bill awaiting realization, purchases in the form of travelers' cheques, currency notes and gift parcels exported every quarter.

(v) R-Returns are being submitted regularly by the branches to RBI who are dealing directly foreign exchange transaction (either purchase or sale of foreign currency) on behalf of that branch or other branches.

Dealing Limits

2.35 The guidelines for dealing limits are discussed below:

Daylight Limits

2.36 The Exchange Control rules requires that the position should be square or near square in each currency at the close of business each day. In the course of operations, during the day both with customer as well as in inter-Bank business, the dealer may have to maintain open positions in the various currencies transacted by the bank. The management should, therefore, lay down the maximum position limits in each currency that may remain uncovered during the day after a careful study of the nature and volume of operations (customer as well as inter-Bank)at each centre at which the bank undertakes inter-Bank operations and the conditions of the exchange markets, generally, both in India and abroad. This necessitates a periodical review (in some circumstances even daily reviews) of the maximum daylight positions permitted to the dealer(s). The need for returning the position to square or near-square is stressed while laying down daylight limits, as the exchange market conditions or the inadequate trading hours or time zone factors make it difficult for the dealer(s) to return to square or near- square position before the close of business. It must be clearly understood that any temporary excesses over the approved daylight position limits will require approval of the bank management. In the smaller banks, its the usual practice even to lay down a dealing limit for the dealer in each currency so that any deal individually larger than the approved limit will require prior approval of appropriate/ designated authority of the bank.

Overnight Limits

2.37 The Exchange Control Rule requiring maintenance of square or near square position is adhered to as the exchange market conditions can be very fluid and unpredictable. Management keeps a close watch on the dealers' positions at the close of business each day - to ensure that the Exchange Control rule supplemented by the internal guidelines is observed. A statement of daily closing positions indicating the overbought and oversold positions, if any, held in excess of the daylight limits in the currency during the day (whatever be the time interval) and the limits (both daylight and overnight) laid down by the management should be submitted to the senior management official at the close of business daily.

2.38 The bank's top management should ensure that the dealers do not hold a position which can be considered as not being near square. Any violations of the Exchange Control regulations in this regard are viewed adversely by the Reserve Bank. Non-reporting days should be effectively curbed through the daily statements submitted to the authorities, supplemented by interval spot checks, wherever necessary.

Inter-Bank Limits

2.39 Authorized dealers should set up limits for dealing with individual banks both in overseas banks as well as authorized dealers in India. While setting up limits, the capital plus reserves position of the other Bank, the manner of past dealings with the Bank and the market reports about the functioning of the Bank must be borne in mind. It is a common practice to lay down limits as a multiple of the last known capital plus the reserves position of the bank. In some cases, balance sheet totals and assets coverage ratios may also be considered while limits are fixed or reviewed. Whatever be the procedure followed, dealings should be undertaken on the basis of value of contracts concluded already and outstanding with the Bank so that the outstanding at all times are within set limits, any temporary excess being permitted with prior consent of the management. For this purpose, sales and purchases must be aggregated and not set off. All transactions, including TOM delivery and SPOT delivery contracts (but not ready or cash) should be reckoned for the purpose of monitoring inter-Bank limits.

Extra care must be exercised if forward maturities get clustered around particular date(s) (months) and the credit risks on the relative settlement dates may be considered.

While banks are free to set limits for the counterpart banks, according to the norms spelled out above they should not fix low limits (including refusal to deal) against particular banks on extraneous considerations such as deposit-grabbing or competition in exchange business.

Customer Limits

2.40 Under the present Exchange Control regulations, all customer contracts for spot deliveries are deliverable on the same day. Further, customer forward contracts are permissible only if they are self-liquidating in nature, i.e., they are fulfilled by delivery of foreign exchange obligations arising from imports of goods or services. Speculative and trading contracts are prohibited. Even then, authorized dealers would do well to set limits for forward contracts for their larger customers so that the credit risks arising from such exposure can be periodically monitored. Such limits may be laid down by the management wherever found appropriate and the monitoring conducted through the accounting department should maintain proper records of customer-wise outstanding liabilities under forward contracts. The transactions of fresh contracts and deliveries there against, handled for such customers, by the Foreign Exchange Department or by the branches should be required to be reported to the Accounting Department to enable it to perform the monitoring function effectively.

Organization of the Dealing Department

General

2.41 Foreign exchange dealing is a highly specialized function and has to be performed by a set of well-trained personnel. Typically, a Dealing Department should consist of dealers and backup staff who are responsible for the follow-up of the deals made by the dealers, giving feedback of collated information to the dealers, helping dealers to get overseas telexes and SWIFTS, checking rates, etc. There is a considerable scope of abuse by over-lapping of functions through manipulation of rates on contracts already concluded manipulation through position, mismatching etc. The effectiveness of control over the dealing room largely depends on how the department is organized. With improvement in communication system, at present, in most of the Banks the Dealing Room is centralised.

Segregation of Dealing and Accounting Functions

2.42 The dealing function must be separated from the accounting, funding and other backup functions. In the smaller banks, the functions should be assigned to different officers of the same rank reporting to a senior officer of the bank, so that the dealing and the backup functions are carried out by two or more persons, mutually supporting and drawing support and each acting as a check on the other in the larger interests of the Bank. The practice observed in certain banks whereby officers in senior ranks handle inter-Bank deals and also control the funding arid other backup functions.

Infrastructure of the Dealing Department

2.43 For the Dealing Department to function effectively, it is necessary that the Managements in the banks provide adequate infrastructure to the Department. Independent telex/SWIFT machines (which can be kept locked by the Dealing Department),which contribute to efficient functioning of the Department, will protect banks from the activities of unauthorized persons with an intention of fraudulent foreign exchange deals on behalf of banks.

Economic journals, newspapers, exchange market reports, reports from leading correspondent banks, money reports from' organizations like Reuters video screen, etc., will greatly enhance the efficiency of the dealers. The larger banks generally provide separate rooms for dealing personnel with proper sound proofing, air-conditioning, stringent access control.

Duties of Dealers

2.44 The duty of the dealers is to operate in the inter-bank market according to the guidelines laid down by the management of the bank from time to time. In the best interests of the bank it is important to provide an effective and quick feedback to the management. The ideal arrangement will be for the dealers to confer before the work starts on the trend in the overnight markets and the markets still operating in the same time zone in the light of the overnight 'news bag' and the Bank's own business and arrive at tentative conclusions valid for the day. The dealer (or the Chief dealer) should keep the management informed of the conclusions.

It is essential that the management should keep communication channels with dealers open at all times (by intercom, direct access, etc.) so that quick consultations are facilitated. In banks operating at various centres under a decentralized set up, the dealers operating at centres away from the Head Office should likewise constantly maintain contact with the local management responsible for the dealer's functions. The dealers could also communicate with the dealer (or the Chief dealer) at the Head Office to coordinate the market view.

Dealing Procedure

2.45 The dealers should have no accounting work of any kind to perform, as they should at all times concentrate on the market through telex, telephones, video screen services, by maintaining contact with other banks, brokers as well as banks abroad. Deals made by the dealers should be recorded on printed 'Deal Slips'.

The deal slips should indicate the name of the broker (if any),name of the counterparty Bank, currency, amount, rate and delivery, under the authentication of the dealer.

2.46 Duplicate deal slips should be prepared preferably indifferent colours to identify sales and purchases. One copy will be retained with the Chief dealer/ Manager and the other, sent to the back-up staff for accounting and issue of contracts etc. Time at which the deal is put through should be invariably indicated in the deal slip. The deal slips should be passed on to the Accounting Department for further processing.

Dealers of Customers Business

2.47 Large banks may find it advisable to deal selectively with customer enquiries regarding rates and also conclude business with them in the Dealing Department, instead of in the Foreign Exchange Department. In such a setup, the dealers attending to customer business should, as far as possible, be distinct from the dealers in inter-Bank in order that the former may have the orientation required for customer dealing which is different from the one required for inter-Bank dealing. Such -separation will also be in the interest of the Bank as possibilities of over familiarity between dealers in the Bank and customers exist.

Rotation of Dealers

2.48 Dealers should not be kept for too long on dealing duties. A period of three to five years being considered as a reasonable period for effecting a change, training and substitution of dealers should be an on-going process so that the same personnel do not remain on dealing duties beyond a reasonable period in the interest of both the individual and the Bank.

Duties of Accounting Department

2.49 For deals done through brokers, the Accounting Department should procure a receipt of exchange broker's notes irrespective of whether the deals have been done through brokers or directly. It is essential for the Accounting Department to confirm deals made by dealers by sending the requisite confirmation of contracts to the counterparty banks. Likewise, the accounting departments should monitor receipt of confirmation of contracts from counterparty banks and check the correctness thereof, by comparison with Deal Slips or the Bank wise record of inter-bank contracts maintained in the department. Confirmation of contracts must be obtained from the counterparty banks in each case. The signature of the official (who should be one other than the dealer)of the counterparty bank should be verified. An official of the Accounting Department authorized in this regard should likewise confirm contracts sent by counterparty banks under his signature.

In no case should the dealer sign the contracts booked by them. Contracts, together with confirmations of counterparty banks should be systematically paired off and after verification inter-send with relative exchange broker's notes (in case of deals made through their medium), filed away in the accounting department for the purpose of record. Discrepancies should be brought to the notice of the dealers and should be rectified on the same day.

2.50 Dealers in the dealing department maintain position pads and funds chart along with the statement of maturity pattern of the contracts. These should be filed in seriatim and kept with the Dealing department for any future reference. They should also keep a track of the 'Nostro' balances on the basis of cable advices received from overseas correspondents. Currency wise positions and funds positions should be communicated at frequent intervals to dealers who would be operating only on the basis of deal slips sent by dealers and the reports of foreign exchange business flowing in from the Foreign Exchange Department and from other reporting branches. On grounds of convenience, the Accounting Department should be situated near the dealers.

2.51 Apart from the position and Funds Records, the Accounting Department maintains all other records to facilitate submission of feedback and control information to dealers on the one hand and the Management of the Bank, on the other. The Accounting Department prepares bank-wise summaries of all outstanding forward exchange contracts with banks for which confirmations from counterparty bank have not been received as on the last working day of each month and have the outstanding confirmed by the counterpart banks.

Chapter 3
Conduct of Concurrent Audit

3.1 A concurrent audit is to be conducted according to the guidelines and instructions given by the particular bank in that regard. However, the basic needs of the Concurrent audits are generally the same in all the banks.

Appointment of Auditor and its Accountability in Terms of RBI Guidelines

3.2 The Reserve Bank of India vide circular DBS.CO.ARS.No. BC. 2/08.91.021/2015-16 dated July 16, 2015 provides as follows in respect of the appointment of a concurrent auditor:

(i) The option to consider whether concurrent audit should be done by Bank's own staff or external auditors (which may include retired staff of its own bank) is left to the discretion of the individual banks.

(ii) In case the bank has engaged its own officials, they should be experienced, well trained and sufficiently senior. The staff engaged in concurrent audit must be independent of the branch where the concurrent audit is being conducted.

(iii) Appointment of an external audit firm may be initially for one year and extended upto three years, after which an auditor could be shifted to another branch subject to satisfactory performance.

(iv) If external audit firms are appointed and any serious acts of omission or commissions are noticed in their working, their appointments may be cancelled and the fact may be reported to RBI and the Institute of Chartered Accountants of India (ICAI).

Appointment Letter and Expectations of the Bank

3.3 When an auditor receives appointment letter as a concurrent auditor of branch from the Bank, he or the firm, as the case may be, is required to communicate his/its acceptance or otherwise through a letter prescribed by the respective Bank. In case, the assignment is accepted, the auditor is also required to submit an undertaking to abide by the terms of appointment as well as regarding confidentiality of Bank's matter besides disclosure of any interest in the Bank and 'Do's and 'Don'ts prescribed by the Bank. This appointment is the agreement between Bank and auditor describing terms of contract, scope of audit and other related terms of reference, such as, time allotted, frequency of checking, etc. The concurrent auditor must mention the reference of this appointment letter in audit programme and letter covering the report.

3.4 In pursuance of extant RBI guidelines, a Bank is required to constitute an Audit Committee of its Board (ACB).The membership of the audit committee is restricted to the Executive Director, nominees of the Central Government and the RBI, Chartered Accountant director and one of the non official directors. One of the functions of this Committee is to provide direction and also oversee the operations of the entire audit function in the Bank. The Committee also has to review the internal inspection/audit function in the Bank, with special emphasis on the system, its quality and effectiveness in terms of follow up. The Committee may also review the system of appointment and remuneration of the concurrent auditor.

3.5 Considering the coverage of this audit assignment and the specialized nature of work there is also a need for training to be imparted to the staff of the auditors. This training has to be given in specialized fields, such as, foreign exchange computerization, treasury functions, latest KYC guidelines, demat activities areas of income leakage, fraud prone areas, determination of credit rating and other similar specialized areas. The Bank can organize such training programmes so that it can ensure the quality of audit.

General Reference

3.6 For the purpose of concurrent audit, the general references should be drawn from the sources, including:

- Bank's Book of Instructions
- Bank's Manual on Documentation
- Circulars of the Reserve Bank of India issued from time to time.
- Exchange Control Manual and Rules of FEDAI (Foreign Exchange Dealers Association of India).
- Inspection Reports of RBI

- Bank's Internal Inspectors Report
- Long Form Audit Report (LFAR) of the statutory auditor
- Visit Reports of Executives from controlling offices*(ZO/HO)*
- *Charge Handling Over Report*

3.7 The concurrent auditor would, therefore need to the following documents in particular before the commencement of the audit.

- The appointment letter together with the management circular/ instruction on the subject.
- Acceptance Letter
- Communication to previous auditor

3.8 A checklist or flow till commencement is given below:

A. On receipt of appointment letter:
   - o Write for No Objection to the immediate previous auditor
   - o Send Acceptance letter along with statement of Fidelity, Confidentiality etc.
   - o Contact the respective Branch Manager – for programme, arrangement and status report

B. To carry with branch during their visit to the branch:
   - o Authorization Letter
   - o Necessary guidelines
   - o Various Formats
   - o Letter head of the branch

C. Audit Programme
   - o Allocation of work
   - o Commencement of the work as per schedule given in subsequent paragraphs

Audit Programme

3.9 The auditor should prepare a audit programme and keep it in the branch concurrent Audit file. After completion of each Monthly/Quarterly audit, the

Progress Report (Annual) should be updated to enable the subsequent concurrent auditor to take up the audit for subsequent months. From the follow-up sheet (indicating what areas are due to be completed), the routine as well as the 'important' areas may be decided during the month and reported under appropriate head of accounts. After completion of drafting of the monthly report, again a 'Follow up' sheet should be prepared for the next month. This process should be continued till the last month of the concurrent audit period. This will ensure that all the areas of the Bank's functioning have been covered by the audit team during the 'concurrent audit year'. In absence of any specific guidelines by the Bank, all credit facilities/ arrangements should be audited at least once during one concurrent audit year.

3.10 The audit programme sheet should emphasize verification of transactions by the concurrent auditors in view of the principal objectives. The concurrent auditor should not confine their areas of functioning to instructions on subject matter already given to them in writing, but should also use their own judgment and wisdom to cover such other matters which might lead to a financial loss subsequently. Each concurrent auditor has to draw his own audit programme. To facilitate them in this task, various items to be verified/audited are listed separately under the handout Concurrent Audit- Induction material. The list is only illustrative and should not be treated as exhaustive. It should be ensured that all other areas (not covered in the Audit Sheet) are comprehensively covered in the Concurrent Audit Report.

3.11 **Understanding the Branch Business Profile** is essential for successful Concurrent Audit of the branch. A model of profile is given below:

Profile of Branch

(i) Name of the Branch :

(ii) Date of Opening of Branch :

(iii) Area Classification – M/U/SU/R :

(iv) Category of Branch – EL/VL/M/S :

(v) Risk – H/M/L :

(vi) Whether Branch is provided with :

- (a) Currency Chest : Yes/No
- (b) SDV : Yes/No

(c) SDL : Yes/No

(d) ATM Facility : Yes/No

(vii) Whether Branch carries out/ has the facility of:

(a) Foreign Exchange Business : Yes/No

(b) Govt. Business : Yes/No

(c) Merchant Banking Business : Yes/No

(d) Mechanisation with CBS (Core Banking System) : Yes/No

(viii) Particulars of the Manager-in-charge of the Branch : Tenure in the Branch

Existing Name Scale From To

Previous

(ix) Date of last internal inspection:

Date of submission of Rectification Confirmation

Date of closure of Report :

(x) Date of last concurrent audit:

Date of submission of Compliance Report/Rectification Confirmation

Date of closure of Report

BUSINESS PROFILE OF THE BRANCH

Name of the Branch…………

For the Month/Quarter ended…………

(a) Synopsis of Assets & Liabilities ₹/Lacs

	Position		
Assets	**As on last day of the financial year**	**As of last day/ Friday of the previous month/quarter**	**As of last day/ Friday of current month/ quarter**
Cash			
Balance with Bank			

Investment			
Advances			
Inter Branch Transaction (Net Dr)			
Other Assets			
P/L/ A/c (Dr. Balance)			
Contra Liabilities for Guarantees/ LCs			
Contra Liability for instruments on collection basis			
Total			
Liabilities			
Deposits			
Borrowing from Banks			
Inter Branch Transaction			
Other Liabilities			
P/L/ A/c			
Contra Liabilities for Guarantees/ LCs			
Contra Liability for instruments on collection basis			
Total			

(b) Business Parameters

	Position	
Particulars	**As of last day/ Friday of the previous month/ quarter**	**As of last day/Friday of current month/ quarter**
Deposits of which low cost deposits		
Deposits at non-card rates		
Advances		
Non-performing Assets (NPA) % to total advances and Fresh NPAs/Recovery performance • of which cash recovery • Other than cash recovery • Priority sector advances Export Credit • Fresh NPAs		
Profit Staff Productivity Observations on sudden spurt or fall in Deposits and Advances.		

Items to be Covered on the First Day of Concurrent Audit

3.12 Generally, on first day of commencing the concurrent audit the following is to be verified by the concurrent auditor along with last Report of the previous Auditor/s:

Cash

3.13 The concurrent auditor should physically verify the cash in hand and it need not be checked very first day but in first few visits. While doing this he should ensure that there is no accumulation of large stocks of heavy cash and cut/mutilated/soiled notes, which otherwise need to be reported. If cash holdings are beyond the prescribed cash retention limit, the same also need to be reported. The concurrent auditor would also need to verify whether cash is promptly remitted to the currency chest or to RBI and need be reported if the same is not being so deposited. The concurrent auditor would also need to check that where cash is remitted, whether, credit for the same is received same day or next day or not and report the same if not so. He also needs to ascertain whether the guidelines for logistics regarding cash remittance are being adhered to.

3.14 Similarly, foreign currency is also to be physically checked by the concurrent auditor and is to be promptly disposed off by selling or by remitting as per direction of the Bank authorities. If accumulated, it needs to be reported. The concurrent auditor also needs to verify whether entire cash is checked physically at least once in a month by the Manager or any other officer other than the Custodian of Cash.

3.15 If heavy cash, more than the retention limit is kept by the branch, that may adversely affect the profitability of the branch in particular and the Bank in general. To avoid it, it is necessary for the branch to keep cash within retention limit, that if there is any theft or robbery in the Bank, that can be claimed from insurance company and there is no loss to the Bank. If cash is found short or excess, that needs to be reported.

Security Forms

3.16 Security forms i.e., Bank draft books, cash order books, FDR books, cheque books, etc. more specifically pre-numbered stationery are to be physically checked with the register/ any other methodology prescribed by the Bank. If any discrepancy is found, that is to be reported.

Government Securities

3.17 Government securities just like NSC, Bonds, etc. held in Bank's own name and Government Securities held against advances are to be physically checked and if any, discrepancy is found, that is to be reported by the concurrent auditor.

Petty Cash, Postage, Telegram, Stamps in Hand/Adhesive Stamps, Travellers' Cheques, Gift Cheques, Articles and Security in Safe Custody

3.18 These are to be physically checked and tallied with General Ledger and if there is any discrepancy, that is to be reported.

Inward Bills for Collection including Parcels, DDs Receivable and Inland Bills Discounted Receivable

3.19 All the inward bills are to be physically checked by the concurrent auditor and all parcels in hand are to be physically verified and if old outstanding bills are kept by the branch beyond the reasonable time after the stipulated time mentioned in bills are to be reported. If bills purchased by any of the other branches of the Bank and received by the branch, and are outstanding beyond stipulated time, the same needs to be reported.

Chapter 4
Prudential Norms for Assets Classification, Income Recognition and Provisioning Pertaining to Advance

Introduction

4.1 Every year, RBI consolidates instructions/ guidelines issued on matters relating to prudential norms on income recognition, asset classification and provisioning pertaining to advances. RBI Master Circular No. DBR.No.BP.BC.2/21.04.048/2015-16 dated July 1, 2015 "Master Circular – Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances" incorporates and updates instructions issued upto 30.06.15.

4.2 The policy of income recognition should be objective and based on record of recovery rather than on any other subjective considerations. Likewise, the classification of assets of banks has to be done on the basis of objective criteria which would ensure a uniform and consistent application of the norms.

4.3 The provisioning should be made on the basis of the classification of assets based on the period for which the asset has remained non-performing and the availability of security and the realizable value thereof.

4.4 As per the above-mentioned RBI Circular, banks are urged to ensure that while granting loans and advances, realistic repayment schedules may be fixed on the basis of cash flows with borrowers. This would go a long way to facilitate prompt repayment by the borrowers and thus, improve the record of recovery in advances.

Non-performing Assets

4.5 An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank. A non-performing asset (NPA) is a loan or an advance where;

(i) Interest and/ or installment of principal remain overdue for a period of more than 90 days in respect of a term loan.

(ii) Overdraft/Cash Credit (OD/CC) accounts remains 'out of order' when, outstanding balance remains continuously in excess of the sanctioned limit/ drawing power for 90 days. In cases where outstanding balance in the principal operating account is less than the sanctioned limit/drawing power, but there are no credits continuously for 90 days as on the date of balance sheet, or credits are not enough to cover the interest debited during the same period (i.e., 90 days).

(iii) the bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted.

(iv) the instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops.

(v) the instalment of principal or interest thereon remains overdue for one crop season for long duration crops.

(vi) The amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitization transaction undertaken in terms of guidelines on securitization dated February 1, 2006.

(vii) in respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.

4.6 In case of interest payments, banks should, classify an account as NPA only if the interest due and charged during any quarter is not serviced fully within 90 days from the end of the quarter. In addition, an account may also be classified as NPA in terms of following paragraph.

Accounts with Temporary Deficiencies

4.7 The classification of an asset as NPA should be based on the record of recovery. Bank should not classify an advance account as NPA merely due to the existence of some deficiencies which are temporary in nature such as:

- Non-availability of adequate drawing power based on the latest available stock statement.
- Balance outstanding exceeding the limit temporarily.
- Non-submission of stock statements
- Non-renewal of the limits on the due date, etc.

4.8 In the matter of classification of accounts with such deficiencies banks may follow the following guidelines:

(i) Banks should ensure that drawings in the working capital accounts are covered by the adequacy of current assets, since current assets are first appropriated in times of distress. Drawing power is required to be arrived at based on the stock statement which is current. However, considering the difficulties of large borrowers, stock statements relied upon by the banks for determining drawing power should not be older than three months. The outstanding in the account based on drawing power calculated from stock statements older than three months, would be deemed as irregular.

A working capital borrower account will become NPA if such irregular drawings are permitted in the account for a continuous period of 90 days even though the unit may be working well or the borrower's financial position is satisfactory.

(ii) Regular and ad hoc credit limits need to be reviewed/ regularized not later than three months from the due date/date of ad hoc sanction. In case of constraints such as non-availability of financial statements and other data from the borrowers, the branch should furnish evidence to show that renewal/ review of credit limits is already on and would be completed soon. In any case, delay beyond six months is not considered desirable as a general discipline. Hence, an account where the regular/ ad hoc credit limits have not been reviewed/ renewed within 180 days from the due date/ date of ad hoc sanction will be treated as NPA.

Asset Classification

4.9 Broadly, advances are categorized into following four heads:

(i) Standard Assets

(ii) Sub-Standard Assets

(iii) Doubtful Assets

(iv) Loss Assets

Standard Assets

4.10 A Standard Asset is one which does not disclose any problem and which does not carry more than normal risk attached to the business. Such an asset is not a non-performing asset.

Sub-standard Assets

4.11 With effect from March 31, 2005, a substandard asset would be one, which has remained NPA for a period less than or equal to 12 months. Such an asset will have well defined credit weaknesses that jeopardize the liquidation of the debt and are characterized by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.

Doubtful Assets

4.12 With effect from March 31, 2005, an asset would be classified as doubtful if it has remained in the substandard category for a period of 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, – on the basis of currently known facts, conditions and values – highly questionable and improbable.

Loss Assets

4.13 A loss asset is one where loss has been identified by the bank; or internal or external auditors ;or the RBI inspection but the amount has not been written off wholly. In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

Income Recognition Policy

4.14 The policy of income recognition has to be objective and based on the record of recovery. Internationally income from non-performing assets (NPA) is not recognized on accrual basis but is booked as income only when it is actually received. Therefore, the banks should not charge and take to income account interest on any NPA. This will apply to Government guaranteed accounts also.

However, interest on advances against Term Deposits, National Savings Certificates (NSCs), Indira Vikas Patras (IVPs), Kisan Vikas Patras (KVPs) and Life Insurance policies may be taken to income account on the due date, provided adequate margin is available in the accounts. Fees and commissions earned by the banks as a result of renegotiations or rescheduling of outstanding debts should be recognized on an accrual basis over the period of time covered by the renegotiated or rescheduled extension of credit.

Reversal of Income

4.15 If any advance, including bills purchased and discounted, becomes NPA, the entire interest accrued and credited to income account in the past periods, should be reversed if the same is not realized. This will apply to Government guaranteed accounts also. In respect of NPAs, fees, commission and similar income that have accrued should cease to accrue in the current period and should be reversed with respect to past periods, if uncollected.

Leased Assets

4.16 The finance charge component of finance income [as defined in 'AS 19-Leases' issued by the Council of the Institute of Chartered Accountants of India (ICAI)] on the leased asset which has accrued and was credited to income account before the asset became non performing, and remaining unrealized, should be reversed or provided for in the current accounting period.

Appropriation of Recovery in NPAs

4.17 Interest realized on NPAs may be taken to income account provided the credits in the accounts towards interest are not out of fresh/ additional credit facilities sanctioned to the borrower concerned. In the absence of a clear agreement between the bank and the borrower for the purpose of appropriation of recoveries in NPAs (i.e., towards principal or interest due), banks should adopt an accounting principle and exercise the right of appropriation of recoveries in a uniform and consistent manner.

Interest Application

4.18 On an account turning NPA, banks should reverse the interest already charged and not collected by debiting Profit and Loss account, and stop further application of interest. However, banks may continue to record such accrued interest in a Memorandum account in their books. For the purpose of computing Gross Advances, interest recorded in the Memorandum account should not be taken into account.

Provisioning Norms

4.19 The primary responsibility for making adequate provisions for any diminution in the value of loan assets, investment or other assets is that of the bank management and the statutory auditors. The assessment made by the inspecting officer of the RBI is furnished to the bank to assist the bank management and the statutory auditors in taking a decision in regard to making adequate and necessary provisions in terms of prudential guidelines.

4.20 In conformity with the prudential norms, provisions should be made on the nonperforming assets on the basis of classification of assets into prescribed categories. Taking into account the time lag between an account becoming doubtful of recovery, its recognition as such, the realization of the security and the erosion over time in the value of security charged to the bank, the banks should make provision against substandard assets, doubtful assets and loss assets as below:

(i) ***Loss assets***

Loss assets should be written off. If loss assets are permitted to remain in the books for any reason, 100 percent of the outstanding should be provided for.

(ii) ***Doubtful assets***

- 100 percent of the extent to which the advance is not covered by the realizable value of the security to which the bank has a valid recourse and the realizable value is estimated on a realistic basis. Auditor should verify whether that security is considered based on the latest information available with the bank.

- In regard to the secured portion, provision may be made on the following basis, at the rates ranging from 25 percent to 100 percent of the secured portion depending upon the period for which the asset has remained doubtful:

Period for which the advance has remained in doubtful category	*Provision requirement (%)*
Up to one year	25
One to three years	40
More than three years	100

Valuation of Security

With a view to bringing down divergence arising out of difference in assessment of the value of security, in cases of NPAs with balance of Rs. 5 crore and above stock audit at annual intervals by external agencies appointed as per the guidelines approved by the Board would be mandatory in order to enhance the reliability on stock valuation. Collaterals such as immovable properties charged in favour of the bank should be got valued once in three years by valuer appointed as per the guidelines approved by the Board of Directors.

(iii) ***Sub-standard assets***

- A general provision of 15 percent on total outstanding should be made without making any allowance for ECGC guarantee cover and securities available.\
- The 'unsecured exposures' which are identified as 'substandard' would attract additional provision of 10 per cent, i.e., a total of 25 per cent on the outstanding balance.

However, in view of certain safeguards such as escrow accounts available in respect of infrastructure lending, infrastructure loan accounts which are classified as sub-standard will attract a provisioning of 20 per cent instead of the aforesaid prescription of 25 per cent. To avail of this benefit of lower provisioning, the banks should have in place an appropriate mechanism to escrow the cash flows and also have a clear and legal first claim on these cash flows.

4.21 The provisioning requirement for unsecured 'doubtful' assets is 100 per cent. Unsecured exposure is defined as an exposure where the realizable value of the security, as assessed by the bank/approved valuers/Reserve Bank's inspecting officers, is not more than 10 percent, ab-initio, of the outstanding exposure.

'Exposure' shall include all funded and non-funded exposures (including underwriting and similar commitments).

'Security' will mean tangible security properly discharged to the bank and will not include intangible securities like guarantees (including State government guarantees), comfort letters etc.

Other Important Issues

4.22 Some other important issues relating to IRAC has been given in brief in the following paragraphs. For further information, it is recommend to refer to the applicable Master Circular issued by the RBI every year.

Accounts Regularised near about the Balance Sheet Date

4.23 The asset classification of borrowal accounts where a solitary or a few credits are recorded before the balance sheet date should be handled with care and without scope for subjectivity. Where the account indicates inherent weakness on the basis of the data available, the account should be deemed as a NPA. In other genuine cases, bank must furnish satisfactory evidence to the auditors about the manner of regularisation of the account to eliminate doubts on their performing status.

Asset Classification to be Borrower-wise and not Facility-wise

4.24 If one facility provided to the borrower becomes a problem (NPA) and not others. Then, all the facilities granted by a bank to a borrower will have to be treated as NPA and not the particular facility which has become irregular.

For NPA classification, auditors need to examine whether all loans of the borrower have been tacked under one customer ID by the bank and also are aggregated properly with respective of being given from various location/divisions of the bank so as to ensure that all the facilities of the borrower are classified as NPA if one of the facilities get classified as NPA as required by RBI guidelines.

4.25 The bills discounted under LC favouring a borrower may not be classified as a Non-performing assets (NPA), when any other facility granted to the borrower is classified as NPA. However, in case documents under LC are not accepted on presentation or the payment under the LC is not made on the due date by the LC issuing bank for any reason and the borrower does not immediately make good the amount disbursed as a result of discounting concerned bills, the outstanding bills discounted will immediately be classified as NPA with effect from the date when the other facilities has been classified as NPA.

4.26 If the debits arising out of devolvement of letters of credit or invoked guarantees are parked in a separate account, the balance outstanding in that account also should be treated as a part of the borrower's principal operating account for the purpose of application of prudential norms on income recognition, asset classification and provisioning.

Advances under Consortium Arrangements

4.27 Asset classification of accounts under consortium should be based on the **record of recovery of the individual member banks** and other aspects having a bearing on the recoverability of the advances. Where the remittances by the borrower under consortium lending arrangements are pooled with one bank and/or where the bank receiving remittances is not parting with the share of other member banks, the account will be treated as not serviced in the books of the other member banks and therefore, be treated as NPA. The banks participating in the consortium should, therefore, arrange to get their share of recovery transferred from the lead bank or get an express consent from the lead bank for the transfer of their share of recovery, to ensure proper asset classification in their respective books.

Erosion in the Value of Security/ Frauds Committed by Borrowers

4.28 In respect of accounts where there are potential threats for recovery on account of erosion in the value of security or non-availability of security and existence of other factors such as frauds committed by borrowers it will not be prudent that such accounts should go through various stages of asset classification. In cases of such serious credit impairment, the asset should be straightaway classified as doubtful or loss asset as appropriate.

- Erosion in the value of securities can be reckoned as significant when the realizable value of the security is less than 50% of the value assessed by the bank or accepted by RBI at the time of last inspection, as the case may be. Such NPAs maybe straightaway classified under doubtful category.
- In case realizable value of security as assessed above is less than 10% of the outstanding in the borrowal account, the existence of security should be ignored and asset should be classified as loss asset. In such cases the assets should either be written off or fully provided for.

Advances against Term Deposits, NSCs, KVPs/IVPs, etc.

4.29 Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs and life policies need not be treated as NPAs, provided adequate margin is available in the accounts. Advances against gold ornaments, government securities and all other securities are not covered by this exemption.

Loans with Moratorium for Payment of Interest

4.30 In the case of bank finance given for industrial projects or for agricultural plantations, etc., where moratorium is available for payment of interest, payment of interest becomes 'due' only after the moratorium or gestation period is over. Therefore, such amounts of interest do not become overdue and hence do not become NPA, with reference to the date of debit of interest. They become overdue after due date for payment of interest, if uncollected.

In the case of housing loan or similar advances granted to staff members where interest is payable after recovery of principal, interest need not be considered as overdue from the first quarter onwards. Such loans/advances should be classified as NPA only when there is a default in repayment of instalment of principal or payment of interest on the respective due dates.

Agricultural Advances

4.31 A loan granted for short duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for two crop seasons.

A loan granted for long duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for one crop season. For the purpose of these guidelines, "long duration" crops would be crops with crop season longer than one year and crops, which are not "long duration" crops, would be treated as "short duration" crops. The crop season for each crop, which means the period up to harvesting of the crops raised, would be as determined by the State Level Bankers' Committee (SLBC) in each State. Depending upon the duration of crops raised by an agriculturist, the above NPA norms would also be made applicable to agricultural term loans availed of by him.

Government Guaranteed Advances

4.32 The credit facilities backed by guarantee of the Central Government though overdue may be treated as NPA only when the Government repudiates its guarantee when invoked. This exemption from classification of Government guaranteed advances as NPA is not for the purpose of recognition of income. The requirement of invocation of guarantee has been delinked for deciding the asset classification and provisioning requirements in respect of State Government guaranteed exposures.

Projects under Implementation

4.33 For all projects financed by the FIs/ banks the 'Date of Completion' and the 'Date of Commencement of Commercial Operations' (DCCO), of the project should be clearly spelt out at the time of financial closure of the project and the same should be formally documented. These should also be documented in the appraisal note by the bank during sanction of the loan.

Takeout Finance

4.34 Takeout finance is the product emerging in the context of the funding of long-term infrastructure projects. Under this arrangement, the institution/the bank financing infrastructure projects will have an arrangement with any financial institution for transferring to the latter the outstanding in respect of such financing in their books on a predetermined basis. In view of the time-lag involved in taking-over, the possibility of a default in the meantime cannot be ruled out. The norms of asset classification will have to be followed by the concerned bank/financial institution in whose books the account stands as balance sheet item as on the relevant date. If the lending institution observes that the asset has turned NPA on the basis of the record of recovery, it should be classified accordingly. The lending institution should not recognise income on accrual basis and account for the same only when it is paid by the borrower/ taking over institution (if the arrangement so provides). However, the taking over institution, on taking over such assets, should make provisions treating the account as NPA from the actual date of it becoming NPA even though the account was not in its books as on that date.

Credit Card Accounts

4.35 In credit card accounts, the amount spent is billed to the card users through a monthly statement with a definite due date for repayment. Banks give an option to the card users to pay either the full amount or a fraction of it, i.e., minimum amount due, on the due date and roll-over the balance amount to the subsequent months' billing cycle.

A credit card account will be treated as non-performing asset if the minimum amount due, as mentioned in the statement, is not paid fully within 90 days from the next statement date. The gap between two statements should not be more than a month. Banks should follow this uniform method of determining over-due status for credit card accounts while reporting to credit information companies and for the purpose of levying of penal charges, *viz*. late payment charges, etc., if any.

Writing off of NPAs

4.36 In terms of Section 43(D) of the Income Tax Act, 1961, income by way of interest in relation to such categories of bad and doubtful debts as may be prescribed having regard to the guidelines issued by the RBI in relation to such debts, shall be chargeable to tax in the previous year in which it is credited to the bank's profit and loss account or received, whichever is earlier.

4.37 This stipulation is not applicable to provisioning required to be made as indicated above. In other words, amounts set aside for making provision for NPAs as above are not eligible for tax deductions.

Therefore, the banks should either make full provision as per the guidelines or write-off such advances and claim such tax benefits as are applicable, by evolving appropriate methodology in consultation with their auditors/tax consultants. Recoveries made in such accounts should be offered for tax purposes as per the rules.

Write-off at Head Office Level

4.38 Banks may write-off advances at Head Office level, even though the relative advances are still outstanding in the branch books. However, it is necessary that provision is made as per the classification accorded to the respective accounts. In other words, if an advance is a loss asset, 100 percent provision will have to be made there for.

NPA Management – Requirement of Effective Mechanism and Granular Data

4.39 Asset quality of banks is one of the most important indicators of their financial health. Banks should, therefore put in place a robust MIS mechanism for early detection of signs of distress at individual account level as well as at segment level (asset class, industry, geographic, size, etc.). Such early warning signals should be used for putting in place an effective preventive asset quality management framework, including a transparent restructuring mechanism for viable accounts under distress within the prevailing regulatory framework, for preserving the economic value of those entities in all segments.

General Principles and Prudential Norms for Restructured Advances

4.40 The following principles and prudential norms are applicable to all advances including the borrowers, who are eligible for special regulatory treatment for asset classifications:

- Banks may restructure the accounts classified under 'standard', 'substandard' and 'doubtful' categories.
- Banks cannot reschedule/ restructure/ renegotiate borrower accounts with retrospective effect. While a restructuring proposal is under consideration, the usual asset classification norms would continue to apply.
- The process of re classification of an asset should not stop merely because restructuring proposal is under consideration.
- Normally, restructuring cannot take place unless alteration/ changes in the original loan agreement are made with the formal consent/ application

of the debtor. However, the process of restructuring can be initiated by the bank in deserving cases subject to customer agreeing to the terms and conditions.

- No account will be taken up for restructuring by the banks unless the financial viability is established and there is a reasonable certainty of repayment from the borrower as per the terms of restructuring package.
- While the borrowers indulging in frauds and malfeasance will continue to remain ineligible for restructuring, banks may review the reasons for classification of the borrowers as willful defaulters.
- BIFR cases are not eligible for restructuring without their express approval.

Chapter 5
Internal Control and Vigil Mechanism

5.1 Internal control moves inversely with chances of irregularities/fraud. This chapter enumerates important areas of such vulnerable transactions where internal control should be effective and adequate. Concurrent auditor should have some insight about it to make the concurrent audit effective. Under Core Banking System, some exceptional reports are generated for daily checking, concurrent auditor has to verify whether these reports have been checked by the branch incumbent/ nodal officers.

5.2 As per RBI Master Directions on "Frauds – Classification and Reporting by commercial banks and select FIs" dated July 1, 2016, in order to have uniformity in reporting, frauds have been classified as under, based mainly on the provisions of the Indian Penal Code:

(a) Misappropriation and criminal breach of trust.

(b) Fraudulent encashment through forged instruments, manipulation of books of account or through fictitious accounts and conversion of property.

(c) Unauthorized credit facilities extended for reward or for illegal gratification.

(d) Cash shortages

(e) Cheating and forgery

(f) Fraudulent transactions involving foreign exchange

(g) Any other type of fraud not coming under the specific heads as above.

These Master Directions specify that during the course of the audit, auditors may come across instances where the transactions in the account or the documents point to the possibility of fraudulent transactions in the account. In such a situation, the auditor should immediately bring it to the notice of the top management and if necessary to the Audit Committee of the Board (ACB) for appropriate action.

5.3 Reporting of frauds to Reserve Bank of India has to be done as per paragraph 3.1 of the abovementioned Master Directions. Banks need not furnish Fraud Monitoring Returns (FMR) 1 in fraud cases involving amount below₹ 0.1 million to RBI in either hard or soft copy. However, banks at their end should make the data entry in respect of such cases through the FRMS package individually in FMR 1 format (less than ₹ 0.1 million) which will get automatically captured in FMR 2 return and will form part of the consolidated database relating to frauds for the respective bank. In respect of frauds above ₹ 0.1 million the following procedure may be adopted:

Name of return	**Amount involved in the fraud**	**Medium in which to be reported**	**To whom it should be reported**	**Timeline for reporting**	**Remarks**
FMR1 Report on actual or suspected frauds	Frauds involving ₹ 0.1 million and above	Soft copy	Central Fraud Monitoring Cell (CFMC), Bengaluru	Within three weeks of detection	A monthly certificate as per Annex –III (mentioning that soft copy of all the FMRs-1 have been submitted to RBI) is to be submitted by the bank to CFMC, Bengaluru with a copy to the respective Regional Office of RBI under whose jurisdiction the Head Office of the bank falls/

					SSM of the bank, within seven days from the end of the month.
Flash report for frauds involving amounts of ₹ 50 million and above.	For frauds involving ₹ 50 million and above.	Hard copy	Through a DO letter addressed to the PCGM/ CGM-in-charge, DBS, RBI, Central Office, Mumbai with a copy to CFMC, Bengaluru	Within a week of such frauds coming to the notice of the bank's head office.	Should include amount involved, nature of fraud, modus operandi in brief, name of the branch/ office, names of parties involved, their constitution, names of proprietors/ partners and directors, names of officials involved and lodging of complaint with police/ CBI.
FMR2 A format of the return is given in Annex II	Quarterly report on frauds outstanding	Soft copy only	CFMC Bengaluru	Within 15 days of the end of the quarter to which it relates	Nil report to be submitted if no fraud is outstanding.

FMR3 A format of the return is given in Annex II	Case-wise quarterly progress reports on frauds involving ₹ 0.1 million and above.	Soft copy only	CFMC Bengaluru	Within 15 days of the end of the quarter to which it relates	Nil report to be submitted if there are no frauds above ₹ 0.1 million outstanding.

5.4 Common fraud-prone transactions are listed below:

(a) Account Opening and Monitoring

(i) Verify whether accounts are opened only after compliance of KYC Norms.

(ii) In newly opened accounts, if there is deposit of large amount of cash/cheque and there is immediate withdrawal of the bulk amount then whether it is being monitored by the management staff.

(iii) Whether introducer's account and signature are duly verified. If letter of thanks is being issued to the introducer, and if so, acknowledged copy of letter of thanks is being held on record. If letter of thanks is not being issued, had the introducer came personally to the bank and had it been duly noted in the specimen signature card.

(iv) In case of reference of customer of different bank branch is obtained, then it should be obtained confidentially without knowledge/assistance of the depositor customer/ introducer.

(v) In dormant/stagnant accounts if any payment is made, whether proper procedure and KYC Norms were adopted. Whether dormancy flag is lifted only after due verification of depositor and necessary KYC verification. Further, such accounts need to be monitored for large transactions in short period.

(vi) Whether specimen signature cards and other documents signed by the customers are kept under dual control always.

(vii) Savings/current deposit passbooks are handled by responsible staff, and there should be no easy access to it by the customers.

(viii) Passbooks deposited for updating are being duly acknowledged.

(ix) Delivery of pass-book is made after scrutiny.

(x) Specimen signature cards of the dormant accounts are segregated and kept under dual control.

(xi) Whether staff account turnovers are scrutinized from time to time by the managerial staff.

(xii) Are Account opening forms kept under effective control.

(b) Remittance

(i) Whether payment of demand drafts/credit authorization notes/credit notes through newly opened accounts are duly monitored by the managerial staff.

(ii) In outward bills collection register (OBC), if outstation instruments, viz., cheques, demand drafts, banker's cheque, refund orders are deposited and on immediate realization are withdrawn from newly opened accounts then are those payments duly monitored.

(iii) In respect of payment of demand draft, pay slip/ banker's cheque/credit authorisation note/credit note, etc. signatures of the authorised signatories are being duly authenticated.

(iv) File for noting number of lost leaves of demand draft, banker's cheque, credit authorization note/credit note, pre-numbered stationery, etc. is maintained and kept readily available for use.

(c) Cash Department

(i) Dual Control System for cash safe/counting of bundles of notes is always maintained.

(ii) Whether cash on hand is properly processed and soiled/mutilated notes are separated as non-issuable notes. Notes with political slogan written over it are also to be separated as non-issuable.

(iii) Separate custody of non-issuable notes to be verified, and timely remittance thereof to the currency chest / zonal office, as per bank's policy to be verified.

(iv) Counterfeit notes to be mentioned in the separate register and proper custody/ preservation thereof needs to be verified.

(v) Dual custody should be maintained for cash transfers from the vault to the counters and vice versa.

(vi) It should be ensured that only requisite amount of cash is transferred to the cash counter/s.

(vii) Generally, fraudulent transactions are made more through payment of cash over counter. Unusual high turnover of cash should be monitored by the managerial staff.

(viii) Statement of SBI/RBI/Focal point branch in relation to maintenance of account, lodgment of cash, etc. is reconciled with that of branch records as routine duty on regular basis. Difference, if any, in between branch record and statement of SBI/RBI/Focal point if persisting for longer period, requires thorough scrutiny and possibility of fraudulent transaction cannot be ruled out.

(ix) Clearing difference adjustment, a/c is being balanced from time to time and no amount is outstanding for long period. The possibility of long outstanding amount may be proved to be fraudulent.

(x) If the cash balance is regularly exceeding the cash retention limit, then suggestion to review the limit should be made, so that insurance part is taken care of properly.

(xi) Over cheque collection counter notice should be displayed that all instruments should be crossed before depositing. Otherwise bearer instruments may be encasehed over the counter of paying bank and the customer concerned may be defrauded.

(xii) There should be no free access to the cash department for other than cash department staff. Cash should not be allowed to be handled by other than cash department staff.

(d) Advance Department

(Term Loan, Demand Loan, Cash Credit, Over Draft A/c, etc.)

(i) Project report, technical viable reports, etc., in respect of advance of large amounts are duly scrutinized and followed up with the borrowers.

(ii) For advance accounts whether pre-sanction and post sanction inspections are carried out and reports are made available for scrutiny.

(iii) In respect of advance made to the companies, ROC compliance is to be verified.

(iv) For vehicle financing, whether charge is registered with the Road Transport Authority and relative charge certificate is held on branch records.

(iv) As per stipulated terms of sanction, whether all the terms, *viz.,* creation of equitable mortgage has been carried out or not. In case of creation of equitable mortgage, whether lawyer's non-encumbrance, valuer's valuation reports, etc., were taken and held on records. If stipulated in the proposal, whether statement of hypothecated/pledged stocks are submitted at the stipulated interval of time, i.e., monthly/bi-monthly/quarterly, etc.

(v) In case of facility against government securities like, KVP, NSC, proper lien has to be marked by issuing authority and the securities invariably be sent through registered post/ speed post by the banker and received back by registered post. In case advance against LIC Policy has been carried out, surrender value must be announced in favor of bank.

(vi) For all types of advance accounts, all documents stipulated in the proposal are executed and these are fully filled in. Blank/ partially filled documents are not acceptable in the court of law. As far as information goes in some banks, it is obligatory for all the documents executed by the borrowers, “Document Checked" stamp is to be affixed on it and it is to be signed by the official in whose presence the documents are executed/signed by the borrower/s.

(vii) Stocks/assets financed by banks are duly insured against all types of risk, i.e., fire, theft, riot, strike and malicious damage, etc. Post sanction inspections are carried out as per stipulated terms of sanction from time to time and the flaws/irregularities pointed out in the reports are duly followed up with the borrowers for redressed measure/s.

(viii) In case of cash credit accounts, the current account/s already opened, if any, of the borrower should immediately be closed except for special reasons, duly approved in this behalf.

(ix) Proper working of drawing power/ limit has to be ensured, based on latest stock statements. Requirement, if any stipulated, of audited stock statement / book debts statement is properly compiled or not.

(xiii) Proper analysis of the latest financial statements to be done and the branch to obtain the explanations for material variations from the borrower.

(xiv) Legal report or proper title clearance certificate, from bank's approved advocate in proper format.

(xv) Latest valuation report (not older than 3 years) from bank's approved valuer to be on the record.

(e) Bills Advance

(i) For regular advance facility, status report of both the drawers and drawer from the bankers should be held on branch records.

(ii) Specific limit are generally granted against documents against Payment (D/P) and Documents against Acceptance (D/A). Clean limits (Bills not accompanied by title to goods) may be D/A or D/P bills and generally clean limits are sanctioned to the borrowers of high integrity and of very large means. Casual limits for bill advance are also granted to the parties of sound financial means.

In case of advance against LIC Policy, surrender value must not be obtained and policy paper must be assigned in favour.

(iii) In case of documentary bills, documents to title to goods, i.e., R/R, B/l, MTR or Lorry Receipts (L/R) should invariably be drawn in favour of Bank or "Drawer of bills", i.e., self. Under no circumstances bills should be drawn in favour of drawers of bills as drawers can retire bills without making payment to banks. For "Self" drawn bills, drawer will endorse the bill in favour of bank.

(iv) Banks have encountered huge amounts of fraud on account of bill business. It is to be verified that bills are drawn out of genuine trade transactions.

(v) In case of huge amounts of outstanding bills, the possibility of fraudulent transactions cannot be ruled out. Overdue bills are retired by purchase/discount of fresh bills in such cases.

(vi) In case of MTR/LR, it is necessary to be examined as to whether the transportation operator concerned is on the approved list of Indian Bank's Association and relative number is mentioned in the consignment note of the Lorry Receipts.

(f) Other Departments

(i) Inter-branch reconciliation - Whether inter-branch reconciliation statement is being attended from time to time and the relative file is made available for scrutiny. It is to be ensured that there is no long outstanding entry pending for unusually long period. Long outstanding entry may be of any fraudulent nature of transaction as instances of frauds have very often come to the surface through outstanding inter branch reconciliation statement. Controlling office may be contacted in case of non-availability of full information in regard to above.

(ii) Suspense, Sundry Deposit, Sundry Credit -These are highly sensitive fraud-prone registers/ledgers. These registers are, generally, monitored by the managerial staff. Any unusual entry requires full investigation and if long outstanding entry is there, the chances of the same as fictitious cannot be ruled out.

(iii) All the originating debit entries in office/ sundry/ suspense debit accounts to be monitored by the branch. Also, the reversal of entries in office/ sundry/suspense credit accounts to be monitored.

(iv) Proper TAT (turnaround time) to be adhered to for office account entries reversal.

(v) Opening and negotiation of bills under Letter of Credit are well within the delegated authority of the branch and, if not, whether permission/sanction of higher authority was available on record. In case of long outstanding bills under L/C, proper verification is necessary.

(vi) For guarantee issued, whether guarantee was issued within the delegated authority and, if not, permission/sanction from higher authority was available on records. In case of invocation of any guarantee, any amount paid is duly reported to the higher authority.

(vii) For guarantees issued, to verify whether all guarantees are issued as per the system, and as per the format approved by the bank's legal cell. Verify whether the appropriate charges have been recovered from the borrower or not.

(viii) On analysis of Profit and Loss Account, it is required to be determined as to whether there are due controls on purchase of stationery/furniture and fixture and these are well within delegated authority of the branch officials. There are due verification/ checking of items of income and expenditure and vouchers are, generally, signed by authorized signatory/signatories.

(ix) Vouchers of the branches are properly counted, totalled, stitched and bundled and total number of vouchers is kept written at the top of voucher lot. Total number of vouchers tallies with that of total number of vouchers recorded in the cash centre book.

(g) Credit Card Transactions

(i) Whether recommendation for issue of credit cards were made after thorough verification of antecedence, income, wealth and necessary verification of the card holders.

(ii) Whether payments received by card holders were timely repaid. If there is outstanding amount due from card holders, then is it being followed up and for long outstanding amounts and also recovery measures are being initiated. Whether higher authorities are informed of outstanding amounts of defaulting card holders.

(iii) Considering incidence of frauds through internet, is there any dispute over the amount of reimbursement claimed for from card holders and is it reported to the higher authority.

Indicative List of Suspicious Activities

5.5 Following is an indicative list of suspicious activities:

(A) Activities not consistent with the customer's business

(i) Corporate accounts where deposits or withdrawals are, primarily in cash rather than cheques.

(ii) Corporate accounts where deposits and withdrawals by cheque, foreign inward remittances and any other means are received from/made to sources apparently unconnected with the corporate business activity /dealings.

(iii) Unusual applications for DD/ TT/ PO against cash.

(iv) Accounts with large volume of credits through DD/ TT/PO whereas the nature of business does not justify such credits.

(v) Accounts with high volume of transactions, with low closing balance.

(vi) Retail deposit of many cheques but rare withdrawals for daily operations.

(B) Attempts to avoid reporting/record-keeping requirements

(i) A customer who is reluctant to provide information needed for a mandatory report, to have the report filed or to proceed with a transaction after being informed that the report must be filed.

(ii) Any individual or group that coerces/induces or attempts to coerce/induce bank employee, and does not files any reports or any other forms.

(iii) An account where there are several cash deposits/ withdrawals below a specified threshold level to avoid filing of reports that may be necessary in case of transaction above the threshold limit, as the customer intentionally splits the transaction into smaller amounts for the purpose of avoiding the threshold limit.

(C) Unusual activities

(i) An account of a customer who does not resides/have office near the branch even though there are bank branches near his residence/office.

(ii) A customer who often visits the safe deposit area immediately before making cash deposits -especially deposits just under the threshold level.

(iii) An account that has frequent deposits of large amounts of currency bearing the labels of other banks.

(iv) Funds coming from the list of countries/centres which are known for money laundering.

(D) Customer who provides insufficient or suspicious information

(i) A customer/company who is reluctant to provide complete information regarding the purpose of the business, prior banking relationships, officers or directors, or its locations. In this case account need not be opened.

(ii) A customer/company who is reluctant to reveal details about its activities or to provide financial statements

(ii) A customer who has no record of past or present employment but makes frequent large transactions.

(E) Certain suspicious funds transfer activities

(i) Sending or receiving frequent or large volumes of cross border remittances.

(ii) Receiving large remittances from various centres and remitting the consolidated amount to different account centre on the same day, leaving minimum balance in the account.

Early Warning Signals

5.6 RBI Master Directions on "Fraud – Classification and Reporting by commercial banks and select FIs" dated July 1, 2016, lists down following early warning signals which should alert the bank officials about some wrongdoings in the loan accounts which may turn out to be fraudulent:

(i) (a) Default in undisputed payment to the statutory bodies as declared in the Annual Report.

(b) Bouncing of high value cheques.

(ii) Frequent change in the scope of the project to be undertaken by the borrower.

(iii) Foreign bills remaining outstanding with the bank for a long time and tendency for bills to remain overdue.

(iv) Delay observed in payment of outstanding dues.

(v) Frequent invocation of BGs and devolvement of LCs.

(vi) Under insured or over insured inventory.

(vii) Invoices devoid of TAN and other details.

(viii) Dispute on the title of collateral securities.

(ix) Funds coming from other banks to liquidate the outstanding loan amount unless in normal course.

(x) In me chanting trade, import leg not revealed to the bank.

(xi) Request received from the borrower to postpone the inspection of the godown for flimsy reasons.

(xii) Funding of the interest by sanctioning additional facilities.

(xiii) Exclusive collateral charged to a number of lenders without NOC of existing charge holders.

(xiv) Concealment of certain vital documents like master agreement, insurance coverage.

(xv) Floating front / associate companies by investing borrowed money.

(xvi) Critical issues highlighted in the Stock Audit report.

(xvii) Liabilities appearing in ROC search report, not reported by the borrower in its annual report.

(xviii) Frequent request for general purpose loans.

(xix) Frequent ad hoc sanctions.

(xx) Not routing of sales proceeds through consortium/ member bank/lenders to the company.

(xxi) LCs issued for local trade / related party transactions without underlying trade transaction.

(xxii) High value RTGS payment to unrelated parties.

(xxiii) Heavy cash withdrawal in loan accounts.

(xxiv) Non submission of original bills for verification upon request.

(xxv) Significant movements in inventory, disproportionately differing vis-a-vis change in the turnover.

(xxvi) Significant movements in receivables, disproportionately differing vis-a-vis change in the turnover.

(xxvii) Disproportionate change in other current assets.

(xxviii) Significant increase in working capital borrowing as percentage of turnover.

(xxix) Increase in Fixed Assets, without corresponding increase in long term sources (when project is implemented).

(xxx) Increase in borrowings, despite huge cash and cash equivalents in the borrower's balance sheet.

(xxxi) Frequent change in accounting period and/or accounting policies.

(xxxii) Costing of the project which is in wide variance with standard cost of installation of the project.

(xxxiii) Claims not acknowledged as debt high.

(xxxiv) Substantial increase in unbilled revenue year after year.

(xxxv) Large number of transactions with inter-connected companies and large outstanding from such companies.

(xxxvi) Substantial related party transactions.

(xxxvii) Material discrepancies in the annual report.

(xxxviii) Significant inconsistencies within the annual report (between various sections).

(xxxix) Poor disclosure of materially adverse information and no qualification by the statutory auditors.

(xl) Raid by Income tax /sales tax/ central excise duty official.

(xli) Significant reduction in the stake of promoter / director or increase in the encumbered shares of promoter/director.

(xlii) Resignation of the key personnel and frequent changes in the management.

Chapter 6
Treasury and Investment Portfolio of Banks

6.1 Fund and investment management is one of the most important and sensitive functions of the bank. The management of the liquidity and investment portfolio of the bank will be under the responsibility of a committee called as "Funds Management and Investment Committee".

The functions of treasury include:

(i) Fund management for the bank being central pool of funds for the bank;

(ii) Maintenance of Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio(SLR);

(iii) Investment functions of the bank;

(iv) Risk management;

(v) Liquidity management;

(vi) Asset Liability Management;

(vii) Participation in forex, money and securities markets;

(viii) Proprietary trading;

(ix) Global cash management;

(x) Managing the cost of funds- NII,NIM,ROA;

(xi) Monitoring the rating migrations.

Audit of Treasury Function

6.2 As per the RBI directives, all treasury transactions are subjected to concurrent audit either by banks internal auditor or by a firm of chartered accountants and the report is placed before the CMD of the bank on monthly basis. The major irregularities observed in these reports and the position of compliance thereto may be incorporated in the half yearly review of the investment portfolio.

Banks should undertake a half-yearly review (as of March 31 and September 30) of their investment portfolio, which should, apart from other operational aspects of investment portfolio, clearly indicate amendments made to the Investment Policy and certify adherence to laid down internal investment policy and procedures and the Reserve Bank guidelines, and put up the same before their respective Boards within a month, i.e., by end-April and end-October.

A copy of the review report put up to the Bank's Board should be forwarded to the Reserve Bank (concerned Regional Office of DBS, RBI) by May 15 and November 15, respectively.

Treasury Audit Approach

6.3 An Illustrative Check List for audit of Treasury and Investment function has been discussed in following paragraphs. The checklist has been bifurcated under various major heads:

Investment Policy

6.4 The auditor should verify that:

(i) There is a clear cut written Investment policy of the bank, duly approved by the board and that it includes quantitative aspects of investment held in its own portfolio. Investment policy outlining the approach, operations products, limits and processes, accounting, valuation, etc., is very important.

(ii) That bank regularly reviews its investment policy and incorporates all the latest guidelines issued by the RBI. Banks should undertake a half-yearly review (as of March 31 and September 30) of their investment portfolio, which should, apart from other operational aspects of investment portfolio, clearly indicate amendments made to the Investment Policy and certify adherence to laid down internal investment policy and procedures, and the Reserve Bank guidelines, and put up the same before their respective Boards within a month, i.e., by end-April and end-October. A copy of the review report put up to the Bank's Board should be forwarded to the Reserve Bank (concerned Regional Office of DBS, RBI) by May 15 and November 15, respectively.

(iii) It ensures per transaction per exposure limit with counter party/brokers, wherever necessary.

(iv) It ensures compliance of credit exposure of the bank to individual/group of borrowers while processing/seeking approval for fresh investment. In this regard, Master Circular – Exposure Norms"" (RBI/2015-16/70 DBR.No.Dir.BC.12/13.03.00/2015-16 dated July 1, 2015) is important.

(v) It ensures compliance of exposure limit to capital market (the aggregate exposure of the bank to the capital markets in all forms has not exceed 40% of its net worth as on March 31 of the previous year and within overall ceiling the banks direct investments should not exceed 20% of its net worth).

(vi) Holding of shares of any company as pledge, mortgagee or absolute owner in compliance of section 19(2) of Banking Regulation Act, 1949, regarding investment in equity shares (No banking company shall hold shares in any company of an amount exceeding 30% of paid up share capital of that company or 30% of bank's share capital and reserves, whichever is less).

(vii) Exposure caps for various investment activities:

- (a) Per entity investments under bonds debentures, commercial paper, certificate of deposits
- (b) Investments in unlisted Non SLR securities- not to exceed 10% of total investments in Non SLR securities as on 31st March of previous year
- (c) Banks must not invest in unrated non-SLR securities (except infrastructure bonds) and fixing of prudential limits
- (d) Cap on NON SLR investments
- (e) Rating migration of the issuers/ issues held in the bank's books and consequent diminution in the portfolio quality
- (f) Per transaction limit for purchase/sale of shares in the secondary market
- (g) Aggregate exposure under MFs
- (h) Exposure limits for Individual borrower and group accounts.

(viii) Bank has a list of approved brokers for debt/capital market and per broker's exposure limit is maintained.

(ix) Neat structure of front, back and middle offices with clear cut roles, responsibilities and duties.

(x) A clear reporting structure and coordinating plan.

(xi) Trading policy describing the trading philosophy, objectives, processes, various limits like, cut loss, dealing limits, etc.

(xii) Composition of investment portfolio as per RBI guidelines and the depreciation on investments, if any, not provided for.

(xiii) System relating to unquoted investments in the portfolio and the liquidity of such investments.

(xiv) System and periodicity of concurrent and internal audit/ inspection of investment activities; follow up on such reports.

(xv) System of recording and accounting of income from investments.

(xvi) System of monitoring of income accrued and due but not received.

(xvii) System of monitoring matured investments and their timely encashment.

(xviii) Average yield on investments.

(xix) Cancelled/amended/ late(C/A/L) booking transactions – complete inventory on these transactions.

Investment Management

6.5 The auditor should verify that:

(i) Investment portfolio is managed in accordance with investment policy objectives and in such a manner that risk is minimized and liquidity is ensured. Investment policy objectives are a) to comply with statutory policy obligations; b) to augment the trading profits and overall yield on investments; c) investments covered under investment policy are SLR securities, Non SLR securities.

(ii) There is a clear segregation of duties between front office/dealing room, back office and mid office.

(iii) Rotation of duties of staff is being done at periodic intervals. Authorized dealers must ensure that the staff concerned in the dealing room understands and abides by the Code of Conduct prescribed by FEDAI and FIMMDA.

(iv) The prudential limits fixed are strictly adhered to by the bank officials.

(v) The SGL statement is reconciled with bank record on monthly basis.

(vi) The dealer is preparing deal slips for each deal which is serially numbered.

(viii) The dealer is adhering to per day/per transaction exposure limit fixed, as per investment policy.

(ix) The dealer is reporting all call/notice/term money market deals on NDS and are reported within 15 minutes in NDS, irrespective of the size of the deal.

(x) The transactions are done within delegated powers and wherever exceeded, confirmation /ratification of actions is taken on record.

(xi) That each time a security is acquired it is recorded whether it is for investment or trading account (HFT,HTM,AFS) and, accordingly, accounted in respective accounts on the basis of laid down accounting policies.

(xii) That investment portfolio is classified into 3 categories of HTM, HFT and AFS. The maximum cap of holding under HTM category, i.e., SLR securities holding under HTM is restricted as per latest RBI guidelines.

(xiii) Position regarding physical verification of securities as of the half year ended September- March is to be certified by the concurrent auditor.

(xiv) Position regarding holding of securities from other centres where the banks securities are held on behalf of the investment department is to be obtained as of the half year ended September and March.

(xv) The statement of securities/stock balance in NDS-OM shall be verified and reconciled with the statements of various securities account, i.e., SGL a/c, CSGL a/c by the concurrent auditors on a daily basis.

(xvi) Management role of various committees - ALCO, Investment, Trading, Risk Review committee and to monitor their performance.

(xvii) Review of investments, trading activities and reports to ACB/ Board.

(xviii) Adherence to regulatory guidelines with respect to treasury deals/structured deals. If branch has acted within HO instructions for purchase and sale of securities.

(xix) Controls around deal modification/cancellation/deletion, wherever applicable.

Repo Transactions

6.6 Banks should follow internal control system and concurrent auditor should ensure that:

(i) Ready forward transactions are undertaken only against the clear balance of securities in gilt account.

(ii) All Repo transactions are promptly reported on the NDS and other terms and conditions referred have been complied with.

(iii) Bank can undertake ready forward transactions only in securities held in excess of the prescribed SLR requirements.

(iv) No sale transaction shall be put through in the first leg of ready forward transaction by CSGL constituent without actually holding the securities in the portfolio.

(v) Double ready forward deals in any security are strictly prohibited.

(vi) All repo/ re-repo transactions should be subject to internal audit and concurrent audit. Violation of the regulatory guidelines, if any, may be brought to the notice of Chief General Manager, Financial Markets Regulation Department, Reserve Bank of India, Mumbai.

Short Sale in Government Securities

6.7 Banks may undertake short sale of central government dated securities subject to the short position being covered within a maximum period of three months including the day of trade.

Short sale is defined as a sale of securities one does not own. A bank can also undertake 'notional' short sale, where it can sell a security short from HFT even if the security is held its AFS/HTM book. Short sale would include 'notional' short sale. The resultant 'notional' short sale position would be subject to the same regulatory requirements as in the case of a short sale.

Cap on short sale:

(i) Illiquid Securities: 0.25 % of the total outstanding stock issued of each security in case of securities

(ii) Liquid Securities: 0.75 % of the total outstanding stock or ₹ 600 cr whichever is lower of each security

A monthly report of short sale transactions on GOI securities duly certified by the concurrent/internal auditors that there were no violations of extant regulatory guidelines on short sale in G securities be submitted to RBI.

6.8 In respect of short sales banks shall ensure adherence to the following:

(i) The sale leg of the transactions should be executed only on the NDS-OM platform. The cover leg of the short sale transaction can, however, be executed either on or outside the NDS-Om platform.

(ii) The sale as well as the cover leg of the transaction should be accounted in the HFT- Held for trading category.

(iii) Short sale transactions shall mark to market on a daily basis and account the resultant gains/losses as per the guidelines for marking to market of the HFT portfolio.

(iv) Under no circumstances, should bank fail to deliver on settlement date, the securities short. Failure to deliver securities short sold shall be treated as an instance of 'SGL bouncing' and bank shall be liable to disciplinary by the RBI.

(v) Banks has been permitted to use the securities acquired under reverse repo to meet the delivery obligation of the short sale obligation.

Engagement of Brokers

6.9 For engagement of brokers to deal in investment transactions, the banks should observe the following guidelines:

(i) Transactions between one bank and another bank should not be put through the brokers' accounts.

(ii) If a deal is put through with the help of a broker, the role of the broker should be restricted to that of bringing the two parties to the deal together.

(iii) With the approval of their top managements, banks should prepare a panel of approved brokers which should be reviewed annually or more often, if so warranted. Clear-cut criteria should be laid down for empanelment of brokers, including verification of their creditworthiness, market reputation, etc. A record of broker-wise details of deals put through and brokerage paid, should be maintained.

(iv) Banks should fix aggregate contract limits for each of the approved brokers. A limit of 5% of total transactions through brokers (both purchase and sales) entered into by a bank during a year should be treated as the aggregate upper contract limit for each of the approved brokers. However, the norm of 5% would not be applicable to banks' dealings through PDs.

(v) The concurrent auditors who audit the treasury operations should scrutinize the business done through brokers also and include it in their monthly report.

(vi) No help of broker is being solicited in inter-bank call money/notice/term money lending and borrowing.

Classification of Investments

6.10 The entire investment portfolio of the banks (including SLR securities and non-SLR securities) should be classified under three categories:

(i) 'Held to Maturity' - The securities acquired by the banks with the intention to hold them up to maturity.

(ii) 'Held for Trading' - The securities acquired by the banks with the intention to trade by taking advantage of the short-term price/interest rate movements.

(iii) 'Available for Sale' - The securities which do not fall within the above two categories.

Bank should decide the category of the investment at the time of acquisition and decision should be recorded on the investment proposals.

Held to Maturity(HTM)

6.11 SLR securities are permitted to be included in HTM. The securities are acquired by the banks with the intention to hold them up to maturity. They need not be marked to market and may be carried at acquisition cost. Permanent diminution should be recognised and it should be provided for each investment. Criteria for recognition of permanent diminution should be based on the happening of an event which suggests that impairment has occurred. This would include:

(i) The company has defaulted in repayment of its debt obligations.

(ii) The loan amount of the company with any bank has been restructured.

(iii) The credit rating of the company has been downgraded to below investment grade.

(iv) When the company has incurred losses for a continuous period of three years and the net worth has consequently been reduced by 25% or more.

(v) In the case of new company or a new project when the originally projected date of achieving the breakeven point has been extended, i.e., the company or the project has not achieved break-even within the gestation period as originally envisaged.

Profit on sale of investments in this category should be first taken to the Profit & Loss Account and thereafter be appropriated to the 'Capital Reserve Account'. Loss on sale will be recognised in the Profit & Loss Account.

Held for Trading (HFT)

6.12 Banks are free to decide the extant of HFT holdings. HFT securities are to be sold within 90 days. If HFT securities are not sold within 90 days, due to exceptional circumstances (such as, tight liquidity, or extreme volatility or market becoming unidirectional), the security should be shifted to the AFS category. Following are some points to be considered:

- Based on banks intent, trading strategies, risk management capabilities, tax planning, manpower skills, capital position.
- The securities acquired by the banks with the intention to trade by taking advantage of the short-term price/interest rate movements.
- Must be compulsory marked to market(MTM) at monthly or at more frequent intervals. Consequently, the book value of the individual securities in this category would also not undergo any change after marking to market.MTM appreciation will be ignored and depreciation will flow straight to P&L. MTM Valuation should be done monthly or at more frequent intervals.

Profit or loss on sale of investments in HFT will be taken to the Profit & Loss account.

Available for Sale (AFS)

6.13 The securities which do not fall within the above two categories must be compulsorily marked to market at quarterly or at more frequent intervals and depreciation will flow straight to PL and MTM appreciation will be ignored.

Portfolio Valuation

6.14 For AFS& HFT investments, a portfolio approach to provisioning may be adopted. Securities under this category shall be valued scrip-wise and depreciation/ appreciation shall be aggregated for each classification of (i) Govt. securities, (ii)other approved securities, (iii)shares, iv)debentures/bonds, (v) Subsidiaries/ joint ventures and (vi)Others (CP, Mutual Fund Units, etc.).

The investment in a particular classification, both in domestic and foreign securities, may be aggregated for the purpose of arriving at net depreciation/appreciation of investments under that category. Net depreciation required to be provided for in any one classification should not be reduced on account of net appreciation in any other classification. This means that net depreciation required to be provided for in any one classification should not be reduced on account of net appreciation in any other classification. Netting off is permitted for intra category and not for inter category. Netting off is not permitted in between AFS and HFT.

Valuation of Investments

6.15 Investments are valued as per RBI guidelines as follows:

- Investments held under HTM category are carried in books at their acquisition cost, premium if any paid on acquisition should be amortised over the period remaining to maturity.
- Available for sale and Held for trading investments are marked to market scrip wise.
- Depreciation/appreciation for each of Government securities, Other approved securities, Shares, Debentures & Bonds, Subsidiaries/ joint ventures and Others (CP, Mutual Fund Units, etc.).
- Classification is aggregated, net depreciation, if any for each classification, is provided for but net appreciation is ignored .Profit or loss on sale of investments in both the categories will be taken to the Profit & Loss Account.

Valuation of Unquoted SLR securities

6.16 Valuation of Unquoted SLR securities should be done as follows:

(i) Central Government Securities-Banks should value the unquoted Central Government securities on the basis of the prices/ YTM rates put out by the PDAI/ FIMMDA at periodical intervals.

(ii) State Government Securities-State Government securities will be valued applying the Yield to Maturity (YTM) method by marking it up by 25 basis points above the yields of the Central Government Securities of equivalent maturity put out by PDAI/ FIMMDA periodically.

(iii) Other 'approved' Securities-Other approved securities will be valued applying the YTM method by marking it up by 25 basis points above the yields of the Central Government Securities of equivalent maturity put out by PDAI/ FIMMDA periodically.

(iv) Treasury bills, commercial papers, certificate of deposits, CBLO, Rural Infrastructure Funds, and investments including share capital deposits of Regional Rural banks are valued at carrying cost.

(v) Unquoted equity shares – Equity shares for which current quotations are not available or where the shares are not quoted on the stock exchanges, should be valued at break-up value (without considering 'revaluation reserves', if any) which is to be ascertained from the company's latest balance sheet (which should not be more than one year prior to the date of valuation). In case the latest balance sheet is not available the shares are to be valued at Re.1 per company.

(vi) Unquoted Mutual Funds Units (MF Units) - Investment in unquoted MF Units is to be valued on the basis of the latest re-purchase price. In case of funds with a lock-in period, where repurchase price/ market quote is not available, units could be valued at Net Asset Value (NAV). If NAV is not available, then these could be valued at cost, till the end of the lock-in period. Wherever the re-purchase price is not available, the units could be valued at the NAV of the respective scheme.

(vii) Investment in securities issued by SC/RC - Lower of the redemption value of the security receipts/ pass through certificates, and the NBV of the financial asset.

(viii) Unquoted Non-SLR securities Debentures/ Bonds - a) The rate used for the YTM for rated debentures/ bonds should be at least 50 basis points above the rate applicable to a Government of India loan of equivalent maturity b)for unrated debentures/ bonds should not be less than the rate applicable to rated debentures/ bonds of equivalent maturity.

(ix) Bonds issued by State Distribution Companies (Discoms) : In case the bonds are not traded and quoted, they will be valued on YTM basis. The relevant YTM will be YTM rates for Central Government Securities of equivalent maturities as put out by FIMMDA on the valuation day with the following mark-ups:

(a) During the period when bonds' liabilities are with the State Discoms and

If guaranteed by respective State Governments – 75 basis points

If not guaranteed by respective State Governments – 100 basis points

(b) During the period when bonds' liabilities are with the respective State Governments – 50 basis points.

Shifting among Categories

6.17 Banks may shift investments to/from HTM with the approval of the Board of Directors once a year "at the beginning of the accounting year." No further shifting to/from HTM will be allowed during the remaining part of that accounting year, except when explicitly permitted by RBI.

In the case of transfer of securities from HTM to AFS / HFT category:

(a) If the security was originally placed under the HTM category at a discount, it may be transferred to AFS / HFT category at the acquisition price / book value.

(b) If the security was originally placed in the HTM category at a premium, it may be transferred to the AFS / HFT category at the amortized cost.

After transfer, these securities should be immediately re-valued and resultant depreciation, if any, may be provided.

If the value of sales and transfers of securities to/from HTM category exceeds 5 per cent of the book value of investments held in HTM category at the beginning of the year, banks should disclose has been in 'Notes to Accounts' in banks' audited Annual Financial Statements.

Transfer of scrips from AFS / HFT category to HTM category should be made at the lower of book value or market value.

6.18 The audit procedures for shifting of investments is as follows:

(i) Obtaining list of shifting of investments during the reporting period, and the approvals obtained thereof.

(ii) Checking compliance with RBI guidelines and existence of proper approvals(BOD/RBI) for same.

(iii) Checking proper recording/ accounting of book value and depreciation on date of shifting.

Non-Performing Investments (NPI)

6.19 In respect of securities included in any of the three categories where interest/ principal is in arrears, banks should not reckon income on the securities and should also make appropriate provisions for the depreciation in the value of the investment. The banks should not set-off the depreciation requirement in respect of these non-performing securities against the appreciation in respect of other performing securities.

An NPI, similar to a non performing advance (NPA), is one where:

(i) Principal/interest remains unpaid for more than 90 days;

(ii) If any credit facility availed by the issuer is NPA in the books of the bank, investment in any of the securities (except preference shares) issued by the same issuer would also be treated as NPA. However, if only the preference shares are classified as NPI, the investment in any of the other performing securities issued by the same issuer may not be classified as NPI and any performing credit facilities granted to that borrower need not be treated as NPA;

(iii) Preference Shares - Dividend unpaid for more than 90 days (even if it is cumulative). If the dividend on preference shares (cumulative or non-cumulative) is not declared/paid in any year it would be treated as due/unpaid in arrears and the date of balance sheet of the issuer for that particular year would be reckoned as due date for the purpose of asset classification;

(iv) Equity Shares -In the event of investment in the shares of the company are valued at Re1 per company on account of non-availability of latest balance sheet, these equity shares would also be reckoned as NPA;

(v) State Government guaranteed investments - When interest/installment of principal or any other amount due to the bank remains unpaid for more than 90 days.

(vi) Bank's investments guaranteed by the Central Government need not be classified as NPI until the Central Government has repudiated the guarantee when invoked. However, this exemption from classification as NPI is not for the purpose of recognition of income.

(vii) In case of conversion of principal and/or interest into equity, debentures, bonds, etc., such instruments should be treated as NPA ab initio in the same asset classification category.

(viii) Security receipts/Pass through certificates which are not redeemed as at the end of the resolution period (5 years or 8 years as the case may be) will be treated as Loss asset in the books of the banks (as per RBI Circular dated 25.2.16).

Impairment

6.20 Banks should recognize any diminution, other than temporary, in the value of their investments in subsidiaries/ joint ventures, which are included under HTM and provide there for. Such diminution should be determined and provided for each investment individually.

On the happening of an event which suggests that impairment has occurred. This would include:

(i) The company has defaulted in repayment of its debt obligations.

(ii) The loan amount of the company with any bank has been restructured(as per IFRS- a restructured asset will be treated as NPA).

(iii) The credit rating of the company has been downgraded to below investment grade.

(iv) When the company has incurred losses for a continuous period of three years and the net worth has consequently been reduced by 25% or more.

(v) New company or the new project has not achieved break even within the gestation period as originally envisaged.

Hardware and Software

6.21 Following are some important points related to hardware and software -

(i) All necessary systems – computer, servers, printers, telephone, fax, internet connections – RTGS, NDS, wire agency connections (as per regulatory prescriptions).

(ii) Physical layout of the dealing room, mid and back office connectivity, stock flow.

(iii) Regulatory connectivity – CCIL, RBI, DAD, PDO connectivity, etc.

(iv) Stock maintenance software, deal market generation, reconciliation, voice recording, etc.

(v) Programs to run the systems as necessary.

(vi) Package to run VaR and other risk measurement tools.

Maintenance of Cash Reserve Ratio by the Bank

6.22 The auditors are required to check and certify that:

(i) Department which computes demand and time liabilities of bank has computed the obligatory CRR for the fortnight correctly and informs funds management department timely for maintenance of CRR.

(ii) There is no default in maintenance of CRR and incase of default whether it has been reported to top management or board.

(iii) Detailed Guidelines for System of compiling Net Demand and Time Liabilities (NDTL) position are given in RBI Master Circular RBI/2015-16/98
DBR.No.Ret.BC.24/12.01.001/2015-16 "Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR)"dated July 1, 2015.

Maintenance of Statutory Liquidity Ratio by the Bank

6.23 The auditors are required to check and certify that:

(i) The bank had correctly computed DTL/NDTL and has maintained required SLR on daily bases and no default has taken place during the period. In case of any default, the same is reported to appropriate authority with amount of penalty paid to RBI.

(ii) Bank is submitting to the RBI before 20th day every month a return in Form VIII showing the amounts of SLR held on alternate Fridays during immediate preceding month with particulars of their DTL.

(iii) Bank is also submitting a statement as annexure to from VIII giving daily position of (a) value of securities held for the purpose of compliance with SLR and (b) the excess cash balance maintained by them with RBI in the prescribed format.

(iv) System of compiling Net Demand and Time Liabilities (NDTL) position.

Borrowings and Lending in Inter-Bank Call Money Market

6.24 The auditors are required to check and certify that following prudential limits for transactions in call/ notice money market as specified by the RBI have been adhered to:

(i) Borrowings - On a fortnightly average basis, borrowing outstanding should not exceed 100% of capital funds (Tier I & Tier II capital) of audited balance sheet. However, banks are allowed to borrow a maximum of 125% of their capital funds on any day during a fortnight.

(ii) Lending - On a fortnightly average basis, lending outstanding should not exceed 25% of their capital funds. However banks are allowed to lend a maximum of 50% of their capital funds on any day during a fortnight.

In this regard, Master Direction on Money Market Instruments: Call/Notice Money Market, Commercial Paper, Certificates of Deposit and Non-Convertible Debentures (original maturity up to one year)(RBI/FMRD/2016-17/32 FMRD. Master Direction No.2/2016-17 July 7, 2016) is important.

Asset Liability Management and Risk Management

6.25 The auditor is expected to make comment on the following aspects:

(i) Existence of Policy on Asset – Liability Management and monitoring thereof; compliance with the RBI guidelines

(ii) Review of MCLR- from 1.4.2016 (marginal cost of fund based lending rate) once in a month

(iii) Risk Management Policy – approach, tools (VaR, PVBP) limits, measurement, monitoring and follow-up. Stop Loss Policy should be approved by the Board.

Sanctioning Authority for Security Transactions

6.26 The auditor should check:

(i) That all transactions in securities are having sanction strictly in accordance with the limits laid down in bank's investment policy;

(ii) That the total exposure in one group of companies is indicated and taken into account while making the investment and these facts are clearly mentioned in the office memorandum seeking sanction from the higher authorities;

(iii) The Repo/Reverse Repo transactions undertaken by the bank under liquidity adjustment facility with RBI through auction process are as per the rules prescribed by the RBI.

Reporting/Review Systems for Security Transaction

6.27 The auditor should verify that:

(i) Daily reports on funds and investment position is put up to top management.

(ii) Monthly sale/ purchase transactions are reported to the Board.

(iii) Balances as per bank's books are reconciled with the balances in the books of Public debt office of RBI.

(iv) All office memoranda for transactions confirmed/sanctioned are serially numbered and are recorded in the register maintained by the bank.

(v) In every Board meeting, a report on funds and treasury management including derivatives giving the position as on the last reporting Friday of every month from the previous Board meeting is placed.

(vi) Checking of application money, reconciliation of SGL account, compliance to RBI norms should be done.

Investments in Privately Placed Instruments

6.28 The auditor should verify that:

(i) The issuer should issue an offer document with terms of issue, authorized by Board resolution.

(ii) Bank shall stipulate entry level ratings, quality standards and industry wise, maturity wise, duration wise, issuer wise limits to mitigate the adverse impacts of concentration and the risk of liquidity.

(iii) Bank shall undertake usual due diligence analysis before making investments in Non SLR securities.

Record Keeping, Monitoring, Reporting, MIS & Statements

6.29 The auditors are required to check and certify that:

(i) There is functional segregation of dealing, settlement and accounting in funds management.

(ii) There exist proper recordkeeping and reporting backed bya strong MIS.

(iii) Review of funds position is periodically done and top management is informed about the positions on daily basis.

(iv) Reviews required by the board are placed within the time frame.

(v) Exposure limits for inter-bank lending with counterparty are reviewed annually and limits fixed.

(vi) RBI's guidelines for valuation of securities for the purpose of SLR is being followed.

(vii) Top management is informed on interest in arrears, securities matured but amount not received and also on the system of follow up for each of these.

(viii) All returns required to be submitted to internal and external agencies have been prepared correctly and submitted timely.

(ix) There is harmonious co-operation and exchange of information between investment department/MIS department and credit department.

(x) Checking of custody of unused BR Forms.

(xi) Use of Bank Receipt (BR).

Derivatives

6.30 The auditors are required to check and certify that:

(i) Board has approved derivate trading policy.

(ii) In case of derivate transactions with clients, treasury will follow. Suitability and appropriateness policy for derivatives guidelines issued by the RBI and FIMMDA.

(iii) Periodic confirmation of Derivative contracts with counterparties.

(iv) Cancellation of forward contracts and passing/recovery of exchange gain/loss.

(v) Gaps and Open position Limit (OPL) maintained in different currencies vis-à-vis prescribed limit for the same. Aggregate Gap limit(AGL) of the Bank is approved by RBI after bank's Board Recommendation. AGL should not exceed 6 times of total capital (Tier I& Tier II) of the bank.Net Open Overnight Position(NOOPL) of the bank should not exceed 25% of total capital (Tier I & Tier II) of the bank.

(vi) Reconciliation of Nostro and Vostro accounts balances in Nostro accounts in different foreign currencies are within the limits prescribed by the bank.

(vii) Collection of underlying documents for derivative and forward contracts. Delays, if any.

(viii) Instances of booking and cancellation of forward contracts with the same counterparty within a span of couple of days or a few days.

(ix) Sample check some of the deals and comments on the correctness of computation.

Disclosure Norms

6.31 The disclosure norms as set out by the RBI should be followed scrupulously. Disclosures are to be made strictly as per the RBI prescribed format and the same are to be got certified by statutory auditors. RBI "Master Circular - Disclosure in Financial Statements - 'Notes to Accounts' "(RBI/2015-16/99 DBR.BP.BC No.23/21.04.018/2015-16 dated July 1, 2015) is important for this purpose.

Compliance

6.32 Following are important aspects with respect to Compliance:

(i) To ensure that the treasury operations of the bank have been conducted in accordance with the instructions issued by the RBI, SEBI from time to time.

(ii) Compliance officer to ensure compliance to regulation and internal guidelines.

(iii) Ensuring compliance to other regulators and correspondence with regulators.

(iv) Sustenance of compliance to various audit observations.

Special-Purpose Certificates Relating to Investments

6.33 Banks require their central auditors to issue the following certificates regarding investments of the bank, in addition to their main audit report and the long form audit report:

(i) Certificate on reconciliation of securities by the bank (both on its own Investment Account as well as PMS clients' account).

(ii) Certificate on compliance by the bank in key areas of prudential and other guidelines relating to such transactions issued by the Reserve Bank of India. RBI Master Circular on "Prudential Norms for Classification, Valuation and Operation of Investment Portfolio by Banks", RBI/2015-16/97 DBR No BP.BC.6/21.04.141/2015-16, dated July 1, 2015 must be adhered to.

Annexure I

Illustrative List of Reports Placed before the Board/Audit Committee of the Board (ACB) with regard to Treasury Function

1	Sale / Purchase of transactions	Board	Monthly
2	Report on Funds Management/Achievement of investment policy objectives.	Board	Monthly
3	Reconciliation of Govt securities (PDO A/c.) with RBI	ACB	Monthly
4	Transactions in equity shares/convertible bonds and debentures/ equity oriented Mutual Funds	ACB	Monthly
5	Capital Market Exposure	ACB	Monthly
6	Report of short sale transactions in GOI securities	Board	Monthly
7	Brokers Exposure Limit	Board	Quarterly
8	Overdue position of SLR/Non-SLR investments	Board	Quarterly
9	Review of Non-SLR investments	Board	Quarterly
10	Information in respect of equity shareholding in borrower companies	ACB	quarterly
11	Review of bank's funds position/statutory requirements and investment portfolio	Board	Half Yearly
12	Review of panel of brokers	Board	Annually
13	Review of investment policy	Board	Annually
14	Transactions with related parties during the financial year	ACB	Annual

Annexure II

Abbreviations

ACB	Audit Committee of the Board
AFS	Available for Sale
CBLO	Collateralized Borrowing and Lending Obligation
CCIL	Clearing Corporation of India Limited
CSGL	Constituent Subsidiary General Ledger
CRR	Cash Reserve Ratio
DVP	Delivery verses Payment Systems
FIMMDA	Fixed Income Money Market and Derivatives Association of India
HFT	Held for Trading
HTM	Held To Maturity
MCLR	Marginal Cost of Fund Based Lending Rate
MTM	Marked to Market
NDS	Negotiated Dealing system
NDS-OM	Negotiated dealing system- Order Matching
NDTL	Net Demand and Time Liabilities
PDAI	Primary Dealers Association of India
PDO	Public Debt Office
REPO	Repurchase Obligation
SGL	Subsidiary General Ledger
SLR	Statutory Liquidity Ratio
STRIPS	Separate Trading of Registered Interest and Principal Securities
RTGS	Real Time Gross Settlement Systems
VaR	Value at Risk

Chapter 7
Foreign Exchange

7.1 All foreign exchange transactions in India are conducted under Foreign Exchange Management Act, 1999 (FEMA) (here in after referred to as "the Act") effective from 1.6.2000 repealing the Foreign Exchange Regulation Act, 1973 (FERA) which was in force since 1.1.1974. FEMA contains 49 sections.

7.2 All forex transactions conducted can be broadly be bifurcated into Current Account Transactions and Capital Account Transactions.

(a) Current account transactions are regular and recurring in nature, *viz*., Export remittances, import remittances, NRI remittances, etc., and rupee is fully convertible on current account transactions. Capital account transactions are those transactions which results in creation of an asset or a liability for a resident overseas or for a non-resident in India. These transactions alter the assets/liabilities position in the balance sheet of the Indian entity.

(b) All current account transactions are free unless restrictions are imposed by Central Government under Section 3 of FEMA. In respect of Current Account transactions, rules are made by Government of India under Section 46 of the Act (five rules have been made so far).

(c) Capital account transactions are permitted unless restricted or imposed by Reserve Bank of India vide Section 6 of the Act. In respect of Capital Account transactions, regulations are made by Reserve Bank of India under Section 47 of the Act and 23 regulations have been made so far.

(d) In terms of Section 10 of the Act, Reserve Bank of India has been authorized to control foreign exchange transactions in India and the Reserve Bank in turn conducts the foreign exchange business through Authorized Persons. Such directions are issued from time to time in the form AP (Dir.) circulars. In addition to these guidelines, Reserve Bank of India and Government of India, periodically, release notifications to effect changes in Capital and Current account transaction, respectively.

(e) The concept of issuing master circulars on 1st week of July every year is now dispensed with and instead Master directions are issued by Reserve Bank of India. Master Directions are issued every year on the first of January consolidating the instructions issued till date and also they are updated as and when changes are made through notifications and / or directions.

It may be noted that so far, seventeen Master Directions were issued as on 1st January, 2016 and updated as and when required (Reference :www.rbi.org.in).

Besides the above Master Directions, the following Master Circulars (as of 1st July, 2016) issued by the Reserve Bank of India are also relevant for understanding the subject of foreign exchange:

- Foreign Investments in India. (No. 15)
- Money Transfer Service Scheme (No. 1)
- Risk Management and Interbank dealings (No. 5)
- Rupee / FC Export credit and customer service to exporters.

  (No. RBI/2015-16/47 DBR No.DIR.BC.14/04.02.002/2015-16 July 1, 2015)

7.3 The following definitions are relevant for understanding the subject of Foreign Exchange:

(a) **Foreign Exchange:**Foreign Exchange means foreign currency, and includes 1) All deposits, credits and balances payable in foreign currency, and any drafts, traveler's cheques, letters of credit and bills of exchange, expressed or drawn in Indian currency and payable in foreign currency,2)Any instrument payable at the option of the drawer or holder, thereof or any other party thereto, either in Indian currency or in foreign currency, or partly in one and partly in the other. Debit cards, ATM cards or any other instrument which can be used to create a financial liability may be defined as currency.

(Section 2 (n) of FEMA,1999)

(b) **Capital Account Transaction:** The following transactions conducted by Person resident in India are treated as Capital Account Transactions as per Schedule I (Regulation 3(1) A of the Act):

(i) Investments in foreign securities.

(ii) Foreign currency loans raised in India and abroad.

(iii) Transfer of immovable property outside India.

(iv) Guarantees issued in favour of a person resident outside India.

(v) Export, import and holding of currency / currency notes.

(vi) Loans and Overdrafts (borrowings) from a person resident outside India.

(vii) Maintenance of foreign currency account in India and outside India.

(viii) Taking out of Insurance policy from an insurance company outside India.

(ix) Loans and overdrafts given to a person resident outside India.

(x) Remittance outside India of capital assets.

(xi) Sale and purchase of foreign exchange derivatives in India and abroad and commodity derivatives abroad.

The following transactions conducted by Person resident in India are treated as Capital Account Transactions as per Schedule II (Regulation 3(1) A of the Act):

(A) Investments in India

- issue of security by a body corporate or an entity in India and investment therein.
- investment by way of contribution to the capital of a firm or a proprietorship concern or an association of persons in India.

(B) Acquisition and transfer of immovable property in India.

(C) Guarantee issued in favour of or on behalf of, a person resident in India.

(D) Import and export of currency notes into/from India.

(E) Deposits between a person resident in India and outside India.

(F) Foreign currency account in India.

(G) Remittance outside India of capital assets in India of a person resident outside India.

(c) **Current Account Transaction** means a transaction other than capital account transaction, but includes the following (section 2(j) of FEMA):

(a) Payment due in connection with foreign trade, other current business, services and short term banking and credit facilities in the ordinary course of business.

(b) Payments due as interest on loans and as net income from investments.

(c) Remittances for living expenses of parents, spouse and children residing a broad, and

(d) Expenses in connection with foreign travel, education and medical care of parents, spouse and children.

(d) **Authorised Person**: Section 2(c) of the Act, states that "authorised person" means an authorised dealer, money changer, off-shore banking unit or any other person authorised under section 10 (1) to deal in foreign exchange and foreign securities. These are authorised by Reserve Bank of India under Section 10 of FEMA to deal in foreign exchange. They are broadly classified as under:

AD CATEGORY I	COMMERCIAL BANKS STATE COOP BANKS URBAN CO OP BANKS	All current and capital account transactions
AD CATEGORY II	UPGRADED FFMCs COOP BANKS RRBS	Non trade related current account transactions specified by Reserve Bank and all activities permitted for FFMC.

AD CATEGORY III	SELECT FINANCIAL AND OTHER INSTITUTIONS	Transactions incidental to the foreign exchange undertaken by them
FFMC (FULL FLEDGED MONEY CHANGERS)	DEPT OF POSTS URBAN COOP BANKS OTHER FFMCs	Purchase and sale of foreign exchange for private and business visits abroad.

The Authorised Dealers (Banks) who have huge network of branches bifurcate their branches into Category A, B and C branches. These branches are allowed to transact in various activities permitted under FEMA. Mostly the assignments will be as under:

(i) CATEGORY A BRANCHES

- Maintains Foreign Currency Accounts in banks abroad and maintains foreign exchange positions.
- Buy / sell foreign currencies in the interbank forex market.
- Provide cover to branches for the forex transactions of their clients.
- Provide forward cover to merchants through their Branches.
- Compliance to RBI / GOI guidelines.
- Provide buying and selling rates to branches.
- Balancing of Nostro Accounts.

The dealing room of the Bank, the Trade Finance Centre of the Bank are the A category Branches.

(ii) CATEGORY B BRANCHES

- Operate foreign currency accounts maintained by category A branches with foreign banks abroad.
- Issue remittances/ demand drafts drawn in foreign currency and also encase for customers.

- Handle exports and import business for the clients.
- Handle all remittance transactions both and current account and capital account transactions.
- Maintain deposit accounts of NRIs such as FCNR, NRE, NRO, EEFC, Diamond Dollar Account, etc.

The B category branches are identified through the AD code (Authorized Dealers Code) issued by the RBI for conducting the foreign exchange business for the customers.

(iii) CATEGORY C BRANCHES

Normally, not allowed to conduct any foreign exchange transactions on their own and route through category B branches. C Category Branches are allowed to open FCNR, NRE, NRO, RFC, EEFC and special foreign currency accounts for their customers.

(e) **Person** includes (i) individual, (ii) a Hindu Undivided family, (iii) a company, (iv) a firm, (v) an association of persons or a body of individuals whether incorporated or not, (vi)every artificial judicial person, not falling in any of the preceding sub-clauses, and (vii)any agency, office, or branch owned or controlled by such person.

(f) **Person Resident in India** means :

(i) a person residing in India for more than 182 days during the course of the preceding financial year, but does not include, a person who has gone out of India or who stays outside India, in either case –(A) (a) for or on taking up employment outside India, or(b) for carrying on outside India a business or vocation outside India or (c) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period.(B) A person who has come to stay in India, in either case, or otherwise than –(a) for or on taking up employment in India, or(b) for carrying on in India a business or vocation in India or (c) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period.

(ii) any person or body corporate registered or incorporated in India.

(iii) an office, branch or agency in India owned or controlled by a person resident outside India.

(iv) an office, branch or agency outside India owned or controlled by a person resident in India. (Section 2 (v) of the Act.)

(g) **Person resident outside India** means a person who is not resident in India. The definition of Non-resident and Person of Indian Origin (PIO) have been defined differently in various guidelines and hence should be guided in that context only.

Similarly, the definition of "relative" should be referred to the context as it has been defined under section 6 of Companies Act, 1956 and Companies Act, 2013, separately.

Current Account Transactions

7.4 Persons resident in India can undertake various current account transactions as per rules framed there under. The detailed rules issued by Government of India are as under:

S.no.	Rule	Details
1	Foreign Exchange Management (Encashment of Draft, Cheque, instrument and payment of interest) Rules, 2000	Deals with these instruments to be delivered to investigating agencies where investigation was referred under section 37 of the Act.
2	Foreign Exchange Management (Authentication of Documents) Rules, 2000	Notifying that the documents received in India and signed by Diplomatic and Consular Officers is treated as notarised.
3	Foreign Exchange Management (Current Account Transactions) Rules, 2000 effective 1.6.2000	Deals with various current account transactions, prohibited, restricted and permitted to persons.
4	Foreign Exchange Management (Adjudication Proceedings and appeal) Rules, 2000	Appointment of Adjudicating authorities for holding inquiry.

5.	Foreign Exchange (compounding proceedings) Rules 2000	Powers of Reserve Bank of India to compound contravention.

7.5 Current Account transactions are permitted under Foreign Exchange Management (Current Account Transactions) Rules, 2000 effective 1.6.2000 (updated from time to time) can be broadly classified into three schedules. Schedule I transaction are strictly prohibited, Schedule II transactions require prior approval of the Central Government and Schedule III transactions are permitted by Authorised dealers within the limits stipulated against each transaction.

(i) Schedule I transactions

The following transactions are prohibited as per Schedule I:

(i) Remittance out of lottery winnings.

(ii) Remittance of income from racing/riding, etc., or any other hobby.

(iii) Remittance for purchase of lottery tickets, banned/prescribed magazines, football pools, sweepstakes, etc.

(iv) Payment of commission on exports made towards equity investment in Joint Ventures/Wholly Owned Subsidiaries abroad of Indian companies.

(v) Remittance of dividend by any company to which the requirement of dividend balancing is applicable.

(vi) Payment of commission on exports under Rupee State Credit Route, except commission up to 10% of invoice value of exports of tea and tobacco.

(vii) Payment related to “Call Back Services” of telephones.

(viii) Remittance of interest income on funds held in Non-resident Special Rupee Scheme account.

In addition to the above, drawl of foreign exchange is prohibited for travel to Nepal and / or Bhutan and a transaction with a person resident in Nepal or Bhutan without Reserve Bank of India approval.

(ii) Schedule II transactions

The following Schedule II transactions require prior approval of Central Government of India:

S.No.	*Purpose of remittance*	*Department to approve.*
1	Cultural Tours	Ministry of Human Resources Development, (Department of Education and Culture)
2	Advertisement in foreign print media for the purposes other than promotion of tourism, foreign investments and international bidding (exceeding USD 10,000) by a State Government and its Public Sector Undertakings	Ministry of Finance, (Department of Economic Affairs)
3	Remittance of freight of vessel chartered by a PSU	Ministry of Surface Transport, (Chartering Wing)
4	Payment of import by a Govt. Department or a PSU on c.i.f. basis (i.e., other than f.o.b. and f.a.s. basis)	Ministry of Surface Transport, (Chartering Wing)
5	Multi-modal transport operators making remittance to their agents abroad	Registration Certificate from the Director General of Shipping
6	Remittance of hiring charges of transponders by (a) TV channels (b) internet service providers	Ministry of Information and Broadcasting Ministry of Communication and IT
7	Remittance of container detention charges exceeding the rate prescribed by Director General of Shipping	Ministry of Surface Transport (Director General of Shipping)
8	Remittance of Prize Money / sponsorship of sports activity abroad	Ministry of HR

	by a person other than Sports bodies if the amount involved exceeds USD 100000	
9	Remittance for membership of P & I club Insurance	Ministry of Finance

(iii) Schedule III transactions

The following Schedule III transactions are effected by the Authorized Dealers, upto the limits specified there of, and all transactions exceeding the limits mentioned therein requires Reserve Bank of India prior approval:

(i) Release of exchange in one financial year for one or more private visits to any country except Nepal and Bhutan.

(ii) Gift remittance for financial year per remitter or donor other than resident individual.

(iii) Donation per financial year per remitter or donor other than resident individual.

(iv) Exchange facilities for persons going abroad for employment.

(v) Exchange facilities for emigration or amount prescribed by country of emigration whichever is lower.

(vi) Remittance for maintenance of close relatives abroad, exceeding net salary (after deduction of taxes, contribution to provident fund and other deductions) of a person who is resident but not permanently resident in India and:

(a) is a citizen of a foreign State other than Pakistan; or

(b) is a citizen of India, who is on deputation to the office or branch or

subsidiary or joint venture in India of such foreign company

(c) exceeding US$1,00,000 per year per recipient, in all other cases.

Explanation : For this purpose a person resident in India on account of his employment deputation of a specified duration (irrespective of length thereof) or for a specific job or assignment, the duration of which does not exceed three years, is a resident but not permanently resident.]

(vii) Release of foreign exchange to a person, irrespective of stay, for business travel, or attending a conference or specialized training or for maintenance of expenses of a patient going abroad for medical treatment or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment or check-up.

(viii) Release of foreign exchange for meeting expenses for medical treatment abroad as per the estimate from the doctor in India or hospital / doctor abroad.

(ix) Release of foreign exchange for studies abroad or upto the estimates given by the institution abroad.

Liberalized Remittance Scheme (LRS)

7.6 The scheme was introduced on February 4, 2004, vide A.P. (DIR Series) Circular No. 64 dated February 4, 2004 read with GoI Notification G.S.R. No.207(E) dated March 23, 2004, as a liberalization measure to facilitate resident individuals to remit funds abroad for permitted current or capital account transactions or combination of both. These guidelines are modified from time to time. As per the scheme, all the above remittances allowed to individuals are subsumed under this scheme. As per the present guidelines, a person can remit upto USD250,000 per financial year to one of those transactions or a combination thereof total not exceeding USD250,000 per financial year. The Scheme is not available to corporate, partnership firms, HUF, Trusts, etc.

7.7 In addition to the above facilities available for remittance to individual persons, the Authorized Dealer is also permitted to make remittances to other than individuals as under. These are not covered under LRS:

1.	Commission, per transaction to agents abroad (for sale of residential flats or commercial plots in India)	25,000 or 5 % of Inward remittance whichever is more
2.	Consultancy services procured from outside India per project. Infrastructure project	1,000,000 10,000,000

3.	Reimbursement in pre-incorporation expenses Remittances exceeding 5 % of investment brought into India or USD 100000 whichever is higher.	100,000
4.	Advertisement Abroad in Media outside India Insurance premium for Health insurance from foreign company. Subscription to magazines. If web services are for the business of the company International Credit Cards.	Fully allowed subject to satisfaction of the Authorised Dealer
5.	Donations not exceeding 1% of foreign exchange earnings during the previous three financial years or USD 5 MN whichever is less for a) Creation of chairs in reputed educational institutes. b) Contributions to funds promoted by educational institutes and c) Contribution to technical institution of the donor company.	USD 5 Million

However, there are no restrictions as to quantum of amount of remittance in respect of the following transaction, subject to that the transaction is to the satisfaction of the authorized dealer, and is as per the guidelines issued by Government of India/ Reserve Bank of India from time to time:

(i) Payments for import of goods.

(ii) Remittance of interest on investment made from abroad.

(iii) Remittance of interest on funds borrowed from abroad.

(iv) Remittance of dividend.

(v) Booking of passage for foreign travel with airline/ shipping companies or booking of cargo in ships/ aircrafts. Indian office can accept payment in rupees and make payment in foreign currency.

(vi) Remittances from RFC / EEFC accounts.

(vii) Export Commission.

(viii) Remittance can be made for payment towards advertisement in print or internet or TV abroad.

(ix) Payment to EOU/SEZ by units in DTA. A EOU/SEZ may supply goods in

(x) units in DTA and DTA can make payment in FC to them which will be credited to FC accounts of SEZ and EEFC of other units.

* All the above are subject to deduction of tax at source and other regulations for respective schemes.

The remitter is required to submit Form A-2 to the Authorized Dealer before making any remittance for the above purposes, if the remittance is above USD25,000 and only a simple declaration form for all the remittances upto USD 25,000 (as per individual Bank's guidelines).

The remittances may also attract provision under section 195 (6) Income Tax Act, 1961, which requires the person paying to NRI to furnish the information. As per Rule 37 BB information should be submitted to Income Tax if paying to a non-resident, not being a company or to a foreign company in Form 15 CA and Form 15 CB.

It is pertinent to note that FEMA guidelines clearly mention that payment of taxes / duties / levies and or any other payments due to any government departments are subject to the individual guidelines issued by the respective departments and constituents availing forex facilities need to abide by those guidelines.

Liberalized Remittance Scheme applicable to Individuals

7.8 The general guidelines are as under:

- Remittances by Resident Individuals upto USD 250,000 per Financial Year for any permitted current or capital account transaction or combination of both.
- The scheme is not available to corporate, partnership firms, HUF, Trusts, etc.
- In case of minor, minor's natural guardian will sign the declaration form.
- Remittances can be consolidated in respect of family members.

- Clubbing is not permitted for capital account transactions such as bank accounts, investment, purchase of property if they are not co-owners/co-partners.
- A resident cannot gift to another resident in foreign currency for the credit of latter's Foreign Currency account abroad under LRS.
- The customer must maintain account with the Bank for a minimum period of one year prior to remittances of capital account transactions.
- Banks should not give any credit facility to resident individuals to facilitate capital account remittances.
- PAN card is mandatory. Upto USD25,000 PAN need not be insisted upon.
- Must designate a specific bank to route all transactions under LRS.
- Must maintain account for a period of one year.
- New customers should produce statement of account of previous bank.

A declaration in specified format should be submitted to the bank. Form A-2 to be filled in. Simple declaration may be obtained upto USD 25000.

7.9 The following capital account transactions are permitted under LRS:

- Opening of accounts abroad with a bank.
- Purchase of property.
- Investment in shares, mutual funds, venture capital funds, unrated debt securities and promissory
- Set up wholly owned subsidiaries and joint ventures.
- Extending loans (FC and Rupee both) to Non Resident Indians who are relatives as defined in Companies Act, 1956.

7.10 The following current account transactions are permitted:

- Includes those listed in Schedule III.
- May allow as Gift to a person residing outside India or as donation to an organization outside India.
- Maintenance of close relative as defined in Companies Act, 1956.
- Objects of art can be purchased.

- Outward remittance can be allowed in the form of DD either in the name of resident individual or in the name of the beneficiary with whom he will be putting.
- Can be used for giving gifts to visiting NRI relatives. The amount should be credited to their NRO accounts.

7.11 The following transactions are prohibited under LRS:

- Remittance for any purpose specifically prohibited under Schedule-I and Schedule II.
- Remittance from India for margins or margin calls to overseas exchanges/ overseas counterparty.
- Remittances for purchase of FCCBs issued by Indian companies in the overseas secondary market.
- Remittance for trading in foreign exchange abroad.
- Remittances directly or indirectly to Nepal, Bhutan, Pakistan and Mauritius.
- Loans can be given to close relatives, close relative as defined in Companies Act, 1956 by way of crossed cheque or electronic transfer within India subject to:

(i) The loan is free of interest.

(ii) Minimum maturity of the loan is one year.

(iii) Should be in the overall limit of USD250000.

(iv) Should be used for personal requirements/ business purposes in India.

(v) Loan should be credited to NRO account.

(vi) The amount shall not be remitted outside India.

(vii) Repayment of the loan should be through inward remittance or debit to NRE/NRO/FCNR accounts of the Non Resident Indian.

Capital Account Transactions

7.12 Person resident in India is allowed to conduct the following transaction with the Authorized Dealer under Capital account subject the limits specified there in.

Sale and purchase of foreign currency

(i) A person travelling abroad can purchase foreign currency not exceeding USD 3000 or its equivalent if he is travelling to any country other than Iraq and Libya in which he is allowed to purchase foreign currency not exceeding USD 5000.In the case of travel to Islamic Republic of Iran Russian Federation and other republics of Commonwealth of independent states entire eligible amount can be carried in currency.

(ii) For travelers proceeding for Haj/ Umrah pilgrimage, full amount of BTQ entitlement (Maximum USD 250,000) in cash or up to the cash limit as specified by the Haj Committee of India, may be released by the ADs and FFMCs.

(iii) Drawl of Foreign currency for any person for travel to Nepal and/ or Bhutan is prohibited. Rupee currency of denomination ₹ 100 and below without any limit and for denominations ₹ 500 and ₹ 1000 can be taken subject to maximum of ₹ 25000.

(iv) The traveler should commence journey not later than 60 days from the sale of foreign currency.

(v) Remittances for tour arrangements, purchase of Euro Rail pass can be given before commencement of journey.

(vi) Unspent currency should be surrendered within 180 days from the date of return. The amount may be sold to AD or held in RFC account or use to discharge a debt or liability in Foreign Currency.

(vii) Unspent cheques be surrendered within 180 days. However, currency upto USD 2000 and unlimited coins can be retained by the traveler on return.

(viii) Unspent foreign currency can be utilized for subsequent journey.

(ix) In case of cancellation of journey entire foreign exchange should be returned.

(x) The unspent money can be credited to Resident Foreign Currency (Domestic) account.

(xi) In all other cases, such as remuneration, income on assets held outside India, inheritance, settlement, gift, tips received in India in foreign currency, should be surrendered within 7 days to Authorized Dealer.

Import of Foreign Currency

7.13 A person coming to India may bring foreign currency without any limit subject to that if the currency notes, travelers' cheques exceed USD 10,000 a declaration in CDF is required, out of which foreign currency notes should not exceed USD 5000.

The person coming to India may also bring Indian currency not exceeding ₹ 25000 per person. From Pakistan and Bangladesh the amount is ₹10000.No such restriction for Nepal and Bhutan except that the denomination should not be above ₹100.

Export of Foreign Currency

7.14 A person going abroad can take outside India other than to Nepal and Bhutan amount not exceeding ₹ 25000 per person. He may take not more than two commemorative coins and export of antique coins are allowed. Gift articles not exceeding value of ₹ 5 lakhs can be sent/ taken along with him. There are no restrictions on carrying jewellery, which are subject to customs guidelines.

Acquiring Foreign Securities

7.15 A person resident in India may acquire foreign securities in the following manner:

- By way of gift from a person resident outside India.
- Issued by a company incorporated outside India under Cashless Employees Stock Option Scheme provided it does not involve any remittance from India.
- By way of inheritance from a person whether resident in or outside India.
- Purchased out of funds held in RFC accounts.
- Bonus shares of the foreign securities held.
- By investing under Liberalized Remittance facility.

Acquisition and Transfer of Immovable Property Outside India

7.16 The following are the cases on acquisition and transfer of immovable property outside India:

(i) A person resident in India can hold, own, transfer or invest in any immovable property situated outside India if such property was acquired, held or owned by him when he was resident outside India or inherited from a person resident outside India**.**

(ii) A person resident in India can receive as gift or inheritance from persons referred above.

(iii) A person resident in India can acquire property through purchase from remittance under LRS/RFC.

For the purpose of these regulations relative means husband, wife, brother, sister or any lineal ascendant or descendant of that individual

(iv) Acquisition or transfer of immovable property outside India bya person resident in India would require RBI permission except when:

(a) property was held outside India by a foreign citizen resident in India.

(b) property acquired by a person or before 8.7.1947 and held with permission of RBI.

(c) property acquired by way of gift or inheritance from Persons referred in (b) above,

(d) property purchased out of funds held in RFC account.

(e) property acquired jointly with a relative who is a person resident outside India provided there is no outflow of funds from India f)property acquired by way of inheritance or gift from a person resident in India who acquired such property abroad as per FEMA guidelines.

Borrowing from Non Resident Indian in Foreign Currency

7.17 Person resident in India is allowed to borrow Maximum amount USD 250,000 from a close relative as defined in Companies Act, 1956 subject to the minimum maturity of the loan is One year and the loan amount has been received as Inward remittance or debit to NRE / FCNR account and no interest is payable on the loan amount.

Borrowing from Non Resident Indian in Rupees

7.18 Person resident in India is allowed to borrow from a non-resident as loan if the amount is received as inward remittance or debit to NRE / FCNR account of the non-resident. The period of loan not to exceed three years and the rate of interest shall not be more than 2% over bank rate. The amount repaid cannot be repatriated, however the same may be allowed to be credited to NRI NRO account.

Investments in Joint Ventures and Wholly Owned Subsidiaries Abroad

7.19 The following are the applicable points:

(i) Indian parties are prohibited from making investment in a foreign entity engaged in real estate (meaning buying and selling of real estate or trading in Transferable Development Rights (TDRs) but does not include development of townships, construction of residential/commercial premises, roads or bridges) or banking business, without the prior approval of the Reserve Bank.

(ii) An Indian party means a company incorporated in India or a body created under an Act of Parliament or a partnership firm registered under the Indian Partnership Act, 1932 or a Limited Liability Partnership (LLP) incorporated under the Limited Liability Partnership Act, 2008, making investment in a Joint Venture or Wholly Owned Subsidiary abroad.

(iii) The Indian party/ entity may extend loan/ guarantee only to an overseas JV / WOS in which it has equity participation.

(iv) The Indian party should not be on the Reserve Bank's Exporters' caution list/ list of defaulters to the banking system.

(v) All transactions relating to a JV/ WOS should be routed through one branch of an Authorized Dealer bank to be designated by the Indian party.

(vi) Investments in Nepal are permitted only in Indian Rupees. Investments in Bhutan are permitted in Indian Rupees as well as in freely convertible currencies.

(vii) Investments in JV/WOS abroad by Indian parties through the medium of a Special Purpose Vehicle (SPV) are also permitted.

(viii) Setting up of an SPV under the Automatic Route is permitted for the purpose of making a investment in JV/WOS overseas.

(ix) Investment in an overseas JV / WOS may be funded out of one or more of the following sources:

(a) Drawl of foreign exchange from an AD bank in India;

(b) Capitalization of exports;

(c) Swap of shares.

(d) Proceeds of External Commercial Borrowings (ECBs)/ Foreign Currency Convertible Bonds (FCCBs)

(e) In exchange of ADRs/GDRs issued in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993, and the guidelines issued there under from time to time by the Government of India

(f) Balances held in EEFC account of the Indian party and

(g) proceeds of foreign currency funds raised through ADR / GDR issues.

Opening of Foreign Currency accounts in India by Person Resident in India

7.20 Person resident in India is permitted to open the following types of accounts maintained in foreign currency. Foreign currency account means an account held or maintained in currency other than the currency of India or Nepal or Bhutan. Relative is a person as defined in section 6 of the Companies Act, 1956. The accounts can be in the form of savings, current or term deposit where the account is an individual and in the form of current or term deposit in other cases. In the case of EEFC, the account will be opened as per the scheme:

(1) Exchange Earners' Foreign Currency Accounts (EEFC)

(2) Resident Foreign Currency Account (Domestic)

(3) Resident Foreign Currency Account

(4) Diamond Dollar Account.

(5) Accounts of SEZ.

(6) Other accounts.

The details of these account are given as under:

(a) Exchange Earners' Foreign Currency Accounts (EEFC)

EEFC account can be opened with 100 percent of the foreign exchange earnings received through inward remittance, payments received in foreign exchange by a 100 per cent Export Oriented Unit for goods supplied to such units or units in DTA, payments received in foreign exchange by a unit in Domestic Tariff Area for supply of goods to a unit in Special Economic Zone (SEZ), counter trade payments, advance remittance received for making exports, professional earnings including director's fees, consultancy fees, lecture fees, honorarium and similar other earnings received by a professional by rendering services in his individual capacity, payments received in foreign exchange by an Indian startup, and/ or re-credit of un-utilised foreign currency earlier withdrawn from the account. However, foreign currency loan raised or investment received from outside India or those received for meeting specific obligations by the account holder cannot be credited to this account.

EEFC account can be used for making payments outside India towards for any capital or current account transactions permitted under Schedule II and III under FEMA, payment in foreign exchange towards cost of goods purchased from a 100 percent Export Oriented Unit, payment of customs duty, trade related loans/ advances, by an exporter account holder to his importer customer outside India, payment in foreign exchange to a person resident in India for supply of goods/ services including payments for air fare and hotel expenditure.

Withdrawal in rupees is permitted from this account, provided the amount so withdrawn cannot be re-credited to the account. The account will be in the form of a non-interest bearing account. The claims settled in rupees by ECGC/ insurance companies should not be credited to the account. The sum total of the accruals in the account during a calendar month should be converted into rupees on or before the last day of the succeeding calendar month after adjusting for utilization of the balances for approved purposes or forward commitments.

Fund-based/ non-fund based credit facilities should not be granted against the balances held in EEFC Accounts. Exporters can repay packing credit advances, whether availed of in rupee or in foreign currency, from balances in their EEFC account to the extent exports have actually taken place.

Balances held in the account may be credited to NRE/ FCNR (B) Accounts, at the option/ request of the account holders consequent upon change of their residential status from resident to non-resident.

(b) Resident Foreign Currency Account (Domestic)

A person resident in India who has gone abroad and acquired foreign exchange payment for services while on a visit to any place outside India:

(i) by way of gift or for service rendered to any person not resident in India while visit to India.

(ii) by way of honorarium or gift while on a visit to any place outside India.

(iii) in the form of unspent amount which he had taken while on visit to a foreign country.

(iv) received as from a relative.

(v) the amount represents disinvestment proceeds of ADR/GDR.

(vi) settlement of Insurance policy claims in Foreign Currency.

The amount kept in the account can be utilized for the purpose of payments towards a current account and capital account transactions. If the person resident in India is going abroad and draws amount under LRS scheme the amount kept under this account shall be drawn over and above his entitlement.

The account shall be maintained in the form of Current Account and shall not bear any interest. There shall be no ceiling on the balances in the account. The sum total of the accruals in the account during a calendar month should be converted into rupees on or before the last day of the succeeding calendar month after adjusting for utilization of the balances for approved purposes.

(c) Resident Foreign Currency Account

Non-resident Indians and PIO who are settling for good in India can open Resident Foreign Current Account with an authorized dealer. A person resident in India is permitted to open a RFC account out of foreign exchange received or acquired by him:

(i) as pension or superannuation benefits from his overseas employer,

(ii) by converting assets which were acquired by him when he was a non-resident or inherited from or gifted by a person resident outside India and repatriated to India,

(iii) received as proceeds of LIC claims/ maturity/ surrendered value settled in forex from an Indian insurance company permitted to undertake life insurance business by the Insurance Regulatory and Development Authority.

The balances in the RFC account are free from all restrictions regarding utilization of foreign currency balances outside India. Such accounts can be held jointly with resident relative as joint holder on 'former or survivor' basis. However, such resident Indian relative joint account holder cannot operate the account during the life time of the resident account holder.

The balances in the Non-Resident External (NRE) Account and Foreign Currency Bank [FCNR (B)] Account can be credited to the RFC account when the residential status of the non-resident Indian (NRI) changes to that of a Resident. The account can be opened as Savings Bank, Current or Term Deposit Account as offered by the Authorized Dealer.

(d) Diamond Dollar Account

Firms and companies dealing in purchase/ sale of rough or cut and polished diamonds/ precious metal jewellery plain, minakari and/ or studded with/ without diamond and/ or other stones with good track record of at least 2 years in import/ export of diamonds/ colored gemstones/ diamond and colored gemstones studded jewellery/ plain gold jewellery and having an average annual turnover of ₹ 3 crores or above during the preceding three licensing years are allowed to open Diamond Dollar Accounts upto five accounts with an authorized dealer. The DDA shall be opened in the name of the exporter and maintained in US Dollars only. The account shall only be in the form of current account and no interest should be paid on the balance held in the account. No intra-account transfer should be allowed between the DDAs maintained by the account holder. Exporter firms and companies maintaining foreign currency accounts, excluding EEFC accounts, with banks in India or abroad, are not eligible to open Diamond Dollar Accounts.

A specific Application in prescribed form by Reserve Bank of India should be obtained while opening these accounts. Permitted credits to the account include following:

(i) amount of pre-shipment and post-shipment finance availed in US Dollars.

(ii) Realizations of export proceeds from shipments of rough, cut, polished diamonds and diamond studded jewellery.

(iii) realization in US Dollars from local sale of rough, cut and polished diamonds.

Permitted debits to the account include:

(i) payment for import/ purchase of rough diamonds from overseas/ local sources.

(ii) payment for purchase of cut and polished diamonds, coloured gemstones and plain gold jewellery from local sources.

(iii) payment for import/ purchase of gold from overseas/ nominated agencies and repayment of US Dollars loans availed from the bank.

(iv) transfer to rupee account of the exporter.

(e) Accounts of SEZ

Units located in SEZ are allowed to foreign currency account with authorized dealer with foreign exchange funds received by the unit. No foreign exchange purchased in India against rupees shall be credited to the account without prior permission from the Reserve Bank.

The funds held in the account shall be used for bona fide trade transactions of the unit in the SEZ with the person resident in India or otherwise. The funds held in these accounts shall not be lent or made available in any manner to any person or entity resident in India not being a unit in Special Economic Zones.

(f) ***Other Accounts***

Persons resident in India are allowed to open foreign currency accounts outside India. Reserve Bank of India permits the following persons to open the accounts:

- By a company for its office / branch.
- For making overseas direct investment.
- Startup Companies.
- Pending utilization of ADR/GDR/ECB funds.
- Students who have gone abroad for studies.
- Residents under LRS Scheme.
- A shipping company incorporated in India.
- Persons who have gone abroad for participation in exhibitions/ fairs.
- Person who has gone on temporary visit abroad.

However, as soon as the purpose for which the account has been opened has been completed, complied, the funds held in these accounts should be immediately repatriated to India. When a person resident in India leaves India for Nepal and Bhutan for taking up employment or for carrying on business or vocation or for any other purpose indicating his intention to stay in Nepal and Bhutan for an uncertain period, his existing account will continue as a resident account. Such account should not be designated as Non-resident (Ordinary) Rupee Account. In terms of Regulation 4(4) of the Notification No.FEMA.5/2000-RB dated May 3, 2000, ADs may open and maintain Rupee accounts for a person resident in Nepal and Bhutan.

Capital Account Transactions for Persons Resident Outside India

Non resident

7.21 The term Non-resident or Non-resident Indian has not been defined in the FEMA. However, Reserve Bank of India has defined the term Non-resident and Non-resident Indian in its various regulations issued from to time. In certain regulations, the term Non-resident Indian includes Persons of Indian Origin also. The following definitions, normally, give an understanding of these two terms - non-resident Indian and Person of Indian Origin. The concept of NRI for the purpose of Income Tax guidelines are different from regulations given by the Reserve Bank of India.

Non-resident Indian means a person resident outside India who is a citizen of India or is a person of Indian origin. This definition holds goods for various regulations issued by RBI namely, Foreign Exchange Management (Deposit) Regulations, 2000, Foreign Exchange Management (Investment in Firm or Proprietary concern in India) Regulations, 2000, Foreign Exchange Management (Transfer or Issue of Security by a person resident outside India) Regulation, 2000.

However, for the purpose of Foreign Exchange Management (Remittance of Assets) Regulation 2000, NRI means a person resident outside India who is a citizen of India.

7.22 Person of Indian Origin (PIO)' is a person resident outside India who is a citizen of any country other than Bangladesh or Pakistan or such other country as may be specified by the Central Government, satisfying the following conditions:

(a) Who was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955 (57 of 1955); or

(b) Who belonged to a territory that became part of India after the 15th day of August, 1947; or

(c) Who is a child or a grandchild or a great grandchild of a citizen of India or of a person referred to in clause (a) or (b); or

(d) Who is a spouse of foreign origin of a citizen of India or spouse of foreign origin of a person referred to in clause (a) or (b) or (c).

Explanation: PIO will include an 'Overseas Citizen of India' cardholder within the meaning of Section 7(A) of the Citizenship Act, 1955

7.23 As FEM (Deposit) Regulations, 2000 have been repealed and replaced by FEM (Deposit) Regulations, 2016 with effect from April 1, 2016 (FEMA 5(R)), the term NRI, wherever it appeared, has been replaced by NRI and/or PIO. Prior to this, PIOs were covered within the definition of NRI.

Facilities available for NRIs and PIOs

7.24 Both NRIs and PIOs can open various deposit accounts with authorised dealers as per guidelines given by Reserve Bank of India from time to time.

A comparative chart of all the deposit schemes are given hereunder:

	FCNR	**NRE**	**NRO**
ELIGIBILITY	NRIs. Residents of Bangladesh/Pakistan nationality/ownership require approval of RBI	NRIs. Residents of Bangladesh/Pakistan nationality/ownership require approval of RBI.	NRIs Residents of Bangladesh/Pakistan nationality/ownership require approval of RBI. In the case of Bangladesh, AD can open provided he has valid visa, and valid residential permit issued by Foreign Registration Office. Foreign Nationals are also allowed to open accounts.
TYPES OF ACCOUNTS	Only Term Deposit Accounts - cumulative or non cumulative.	Savings Bank and Current Accounts, TDR accounts cumulative or non	All types of accounts allowed including Current Deposit Accounts.

	Accepted in permitted currency which is fully convertible. For example : USD, GBP, EUR, AUD. (Some banks accept additional currencies also)	cumulative, RD accounts allowed. Remittance can be received in any currency but the account maintained in Indian Rupees.	Remittance can be received in any currency and also some local credits allowed. Maintained in Indian Rupees.
PERIOD OF DEPOSIT ANDRATE OF INTEREST	**PERIOD** Minimum 1 year. Maximum 5 years. **RATE OF INTEREST** 1 to < 3 yrs – LIBOR + 200 bps. 3 to 5 yrs – LIBOR + 300 bps. LIBOR given by FEDAI monthly.	**PERIOD** TDRs Minimum one year. Maximum 10 years. **RATE OF INTEREST** As decided by individual Banks. ROI should not be more than domestic deposits.	**PERIOD** TDRs Minimum 7 days. Maximum 10 years as applicable to domestic deposits. **RATE OF INTEREST** As decided by individual banks. Rates as applicable to domestic deposits.
JOINT ACCOUNTS	Individuals, two or more NRIs Individuals. Joint Account with Resident close relative on F or S basis.	Individuals, two or more NRIs Individuals. Joint Account with Resident close relative on F or S basis.	Individuals, two or more NRIs. Joint account can be opened with NRIs and / or Indian Residents. Operational instructions, E or S, F or S, or Any or

	NO Income Tax on interest	NO Income Tax on interest	S. Tax at 30.9% to be deducted on interest. In case DTAT countries appropriate tax will be deducted.
NOMINATION	NRI / RESIDENT ALLOWED. In the event of demise of the account holder, the balances in the account can be transferred to the non resident nominee. If a resident nominee requests for remittance of funds outside the country to meet the liabilities of the NRI, RBI permission is required. Allowed in any currency	NRI / RESIDENT ALLOWED. In the event of demise of the account holder, the balances in the account can be transferred to the non resident nominee. If a resident nominee requests for remittance of funds outside the country to meet the liabilities of the NRI, RBI permission is required. Allowed in any currency.	NRI / RESIDENT ALLOWED. In the event of demise of the account holder, the balances in the account can be transferred to the non resident nominee. If a resident nominee requests for remittance of funds outside the country to meet the liabilities of the NRI, RBI permission is required.
REPATRIATION OF FUNDS			Allowed with restrictions. i) Current Income and Interest.

			ii) Upto USD 1 Mn. per financial year for any bonafide purposes / sale proceeds of assets.
POWER OF ATTORNEY	Allowed for repatriation of funds to depositor.	Allowed for repatriation of funds to depositor.	Allowed for repatriation of funds to depositor Local Payments. Remittances outside India from current income in India.
I NTERNATI-ONAL CREDIT CARDS	International Credit card can be given to all NRIs.	International Credit card / Debit Card / Cheque Books for SB accounts.	International Credit card / Debit Card / Cheque Books for SB accounts.
PERMISSIBL E CREDITS	Inward remittance for creation of the deposit	Inward remittance. Interest accrued on the account. Interest on investment. Transfer from other NRE/FCNR accounts. Current income like rent, dividend, pension, interest etc.	Inward remittances. Legitimate dues in India. Rupee gift / loan given by a resident under LRS Scheme.

PERMISSIBLE DEBITS	Repatriation funds on maturity of the deposit. Transfer funds to NRE / NRO account. Meeting local payments in Indian rupees	Local payments. Remittances outside India. Transfer to NRE/FCNR accounts.	Local payments. Transfer of current income abroad (over and above USD one million) Upto USD 1 Mn. per financial year for any bonafide purposes / sale proceeds of assets. Funds can be transferred to NRE account within this USD 1 million.
LOANS IN INDIA IN RUPEES AGAINST TDRS	Account Holder / Third Party Allowed	Account Holder / Third Party Allowed	Account Holder / Third Party Allowed
LOANS IN FOREIGN CURRENCY AGAINST TDRS	Account Holder / Third Party Allowed	Account Holder / Third Party Allowed	NOT PERMITTED
PURPOSE OF LOAN	Personal purposes or for carrying on business activities Direct investment in India on non-repatriation basis by way of contribution to the capital of Indian	Personal purposes or for carrying on business activities Direct investment in India on non-repatriation basis by way of contribution to the capital of Indian firms / companies	Personal requirement / Business purpose. Loan cannot be sanctioned for relending, carrying on agricultural/ plantation activities or investment in real estate.

	firms / companies Acquisition of flat / house in India for his own residential use.	Acquisition of flat / house in India for his own residential use.	

Guidelines for Loans against NRI Deposits

7.25 Authorised Dealers/ banks in India can grant loans against the security of the funds held in NRE accounts to the account holder/ third party in India, without any limits, subject to the usual margin requirements. The loan cannot be repatriated outside India and shall be used for the following purposes:

a) personal purposes or for carrying on business activities except for the purpose of relending or carrying on agricultural/ plantation activities or for investment in real estate business;

b) making direct investment in India on non-repatriation basis by way of contribution to the capital of Indian firms/ companies subject to the provisions of the relevant Regulations made under the Act;

c) acquiring flat/ house in India for his own residential use subject to the provisions of the relevant Regulations made under the Act.

In case of loans sanctioned to a third party, there should be no direct or indirect foreign exchange consideration for the non-resident depositor agreeing to pledge his deposits to enable the resident individual/ firm/ company to obtain such facilities.

In case of the loan sanctioned to the account holder, it can be repaid either by adjusting the deposits or through inward remittances from outside India through banking channels or out of balances held in the NRO account of the account holder.

Authorised Dealers may allow their branches/ correspondents outside India to grant loans to or in favour of non-resident depositor or to third parties at the request of depositor for bona fide purpose against the security of funds held in the NRE accounts in India and also agree for remittance of the funds from India, if necessary, for liquidation of the outstanding.

The facility for premature withdrawal of deposits will not be available where loans against such deposits are availed of. The term "loan" shall include all types of fund based/ non-fund based facilities. Loans against security of immovable property or shares can be allowed to NRIs in India rupees. However, the purpose of loan should be for meeting personal expenses. The amount cannot be credited to NRE / FCNR accounts and no repatriation is allowed. The repayment of these loans should be through inward remittance or to the debit of NRE / FCNR account.

Investment in Shares and Securities

7.26 A Non- Resident Indian (NRI) may acquire securities or units on a Stock Exchange in India on repatriation basis under the Portfolio Investment Scheme, subject to the terms and conditions specified in Schedule 3. A Non- Resident Indian (NRI) may acquire securities or units on a non-repatriation basis, subject to the terms and conditions specified in Schedule 4.

For this purpose, the NRI is required to open a special account called NRE (PIS) account with an authorised dealer who is offering such accounts.

Acquisition and Transfer of Property in India

7.27 These guidelines are applicable to both Non-resident Indians and Persons of India Origin.NRI can acquire property in India by:

(i) purchase of immovable property (other than agricultural land/plantation property /farm house) and

(ii) Transfer of immovable property. (Transfer includes sales, purchase, mortgage, exchange, pledge, gift, loan or any other form of transfer of right, title, possession or lien). Incase the residential property so purchased is sold, the purchase price can also be permitted to be repatriated and the balance amount has to be credited to NRO account and such repatriation is allowed only in the case of two properties.

In case property is purchased through rupee funds an amount upto USD 1 Mn is allowed to be repatriated in a financial year after obtaining permission from Reserve Bank of India. In case property in India has been acquired while the status of the NRI remains as NRI, an amount upto USD 1 Mn is allowed to be repatriated in a financial year after obtaining permission from Reserve Bank of India.

Incase property has been acquired while the status of the NRI was person resident in India, RBI permission is required to repatriate the funds.

The NRI is allowed to transfer the property held in India to a person resident in India, or another NRI, PIO. But transfer of property to foreign national is not allowed.

Other Remittance Facilities for NRIs / PIOs

7.28 Current income like rent, dividend, etc., can be remitted outside India and the same can also be credited to NRE ac. They are also permitted to remit upto USD 1 Mn. per year funds held in NRO ac/sale proceeds of immovable property purchased by him out of rupee funds or acquired through inheritance without any lock in period. However, this facility is not available for citizens of Pakistan, Bangladesh, Sri Lanka, China, Afghanistan, Iran, Nepal and Bhutan.

Foreign Nationals

7.29 Foreign nationals of non-Indian origin on a visit to India can open NRO – CD/ SB accounts for a maximum period of six months. Funds should be received through Banking channels. This facility is not for citizens of Nepal and Bhutan. On return of the foreign national, the funds can be repatriated subject to account has been maintained for a period not exceeding six months and the account has not been credited with any local funds, other than interest accrued thereon. RBI approval required for accounts above six months.

Foreign nationals of non-Indian origin resident outside India cannot acquire any property in India unless such property is acquired by way of inheritance from a person who was resident in India. They can acquire on lease for five years without permission from RBI.

7.30 Citizens of Pakistan, Bangladesh, Sri Lanka, Afghanistan, China, Iran, Nepal, Bhutan, Macau or Hong Kong cannot, without prior permission of the Reserve Bank, acquire or transfer immovable property in India, other than lease, not exceeding five years.

Foreign nationals resident in India can open and maintain resident rupee accounts. On return, their accounts should be re-designated as NRO to enable pending funds to be credited to the account. On retirement from India, they are permitted to remit USD 1 Mn from his NRO account every year. They have been, however, permitted to maintain a foreign currency account outside India and remit his salary to that account.

Requirements under Income Tax Act

7.31 Section 195 (6) of Income Tax Act, 1961, requires the person paying to NRI to furnish the information as per Rule 37 BB. Information should be submitted to Income Tax if paying to a non-resident, not being a company or to a foreign company in FORM 15 CA AND 15 CB.

Import of Goods and Services

7.32 In addition to Exchange Management controlled by Reserve bank of India in respect of import of goods and services, one should be familiar with trade management guidelines governing the imports. It is also necessary that one should be familiar with the internal guidelines of the Bank as major areas like, assessment of limits, obtention of securities, documentation, interest rates and service charges, opening of Letters of Credit, issuance of guarantee, standby letters of credit are governed by internal guidelines of each bank. One should also be familiar with ICC guidelines governing Letters of Credit – Uniform Customs and Practices - UCP600, Standby Letters of Credit – ISBP 98, Uniform Rules for Collection – URC 522, Uniform Rules for Demand Guarantees – URDG 758, INCOTERMS 2010, etc.

Guidelines under Trade Control

7.33 Both imports and exports are controlled by Ministry of Commerce and Industry through Director General of Foreign Trade (DGFT). Government of India releases Foreign Trade Policy (FTP) which is applicable for a period of five years and the present policy is for the period 2015-20. As per the FTP policy guidelines, any person conducting the business under imports and exports should first have IEC number obtained from DGFT. All items are classified as those which may be freely imported, restricted, canalized or prohibited. Authorized Dealers may freely open Letters of Credit and allow remittances for import of goods unless they are included in the restrictive list requiring license under the Foreign Trade Policy in force. In such cases, letters of credit should be opened only against valid import licenses marked "For Exchange Control Purposes".

Reserve Bank of India Guidelines on Import of Goods and Services

7.34 The authorised dealers who are conducting transactions for importers must ensure that the importer has obtained valid IEC (Import-Export Code) number from DGFT. The goods being imported if categorised under restricted category needs licence issued by DGFT and a copy marked as "for Exchange Control purposes" has been obtained and kept on record. The banks should also ensure that the Importer holds a confirmed order executed between the importer and supplier of goods. The branches should meticulously follow KYC guidelines issued by RBI from time to time regarding opening, monitoring and scrutinizing the transactions of importers. Branches should obtain a declaration in FORM-1, when the importer/ exporter regularly deal with the bank and to be obtained once. In case the dealings of importer are occasional or casual in nature FORM – II should be obtained. Whenever payments are required to be made by Authorised Dealer, the importer is required to submit his request in FORM – A – 1 which has been since dispensed with by Reserve Bank of India. However, a suitable declaration should be obtained with proper supporting documents.

7.35 Banks are required to make payments for importers in respect of import transactions in the following circumstances:

(i) Payments towards receipt of bills under Letter of credit opened by them on behalf of the importer favouring foreign supplier/ bank.

(ii) Advances remittances for imports as required by the supplier.

(iii) Payment towards realization of bills received under collection from the Seller /his bank.

(iv) Out ward remittances for direct imports.

Settlement of Import Payments

7.36 All import payments, normally, should be settled within a period of six months from the date of shipment. In case of delayed settlement, Authorized Dealer can allow payment of interest upto 3 years. Extension in period of payment should be given 6 months at a time. Incase extension is given beyond one year, the total outstanding of the importer does not exceed USD one Mio or 10% of the average import remittances during the preceding two financial years, whichever is lower. There is no time limit for payment of import of books.

Interest payment may be made incase payments are made later. The Authorized Dealer should be satisfied of such delayed payment. Importer may withhold 15% from import payments as per the terms of purchase agreement between the importer and the seller. This may be paid without interest later.

Trade Credits

7.37 In case deferred payment arrangements, such as, Suppliers' and Buyers' credit are made by the importer such payments are covered under Trade Credits. In case of trade credits (which are covered under ECB guidelines) the maximum amount allowed is USD 20 MN, upto one year for non-capital goods and upto 5 years for Capital Goods per import transaction in all sectors from date of shipment.

Incase trade credit has been sanctioned no rollover/extension is permitted. The all in cost for payment of Interest should not exceed 6 months LIBOR + 350 bps. AD is permitted to issue guarantee for payment of trade credits upto a period of 3 years.

Third Party Payments for Imports

7.38 Sometimes the importers may require to make payments to third party who is other than the seller of the goods. In such cases third payment payments are allowed subject to a firm irrevocable purchase order / tripartite agreement is in place between the importer, seller and the third party (normally, the supplier of goods) and authorized dealer is satisfied with the bonafide of the transactions and should consider the Financial Action Task Force (FATF) statement before handling the transactions. The Invoice should contain a narration that the related payment has to be made to the (named) third party. Bill of Entry should mention the name of the shipper as also the narration that the related payment has to be made to the (named) third party.

Advances Remittances

7.39 The seller may request the importer to arrange for advance remittance after execution of purchase order and before shipment of the goods. Authorized dealers may entertain such requests from importer customers subject to (i) the importer holds a valid import license if license is required for such import, (ii) a confirmed order is in place between the supplier and the importer, (iii) advance remittance is made directly to supplier. The AD banks may not insist guarantee from the supplier's bank upto an amount of advance remittance of USD 200,000. Incase the amount exceeds USD 200,000 guarantee from International bank provided by the supplier is required. Individual Banks may waive the condition and make payment upto USD 1 Mn as per their Board approved policy. A declaration should be obtained as per Bank's performa.

Advance Remittances for Import of Rough Diamonds

7.40 The authorized dealer before making advance remittance for an importer who is dealing in import of rough diamonds must ensure that (i) the overseas mining company has the recommendation of GJEPC (The Gem and Jewellery Export Promotion Council.) (ii)The importer should be a recognized processor of rough diamonds and should have a good track record, (iii)AD Category - I banks should, undertake the transaction based on their commercial judgment and after being satisfied about the bonafides of the transaction, (iv)Advance payments should be made strictly as per the terms of the sale contract and should be made directly to the account of the company concerned. Further, due caution should be exercised to ensure that remittance is not permitted for import of conflict diamonds (Kimberly Certification) and KYC and due diligence exercise should be done. Banks should follow-up submission of the Bill of Entry / documents evidencing import of rough diamonds into the country by the importer.

Time Period for Shipment/ Payment Under Advance Remittances

7.41 Goods should be imported within 6 months from the date of advance remittance for noncapital goods and 3 years for capital goods. The authorized dealer can allow an extension of one month for import of goods. In case of non-import, the advance payment if any made should be repatriated immediately. The balance amount of remittances for imports should be completed within six months from the date of shipment.

Procedure for Receipt of Import Bills/ Documents (otherwise than under Letter of Credit)

7.42 Sometimes, as per the purchase order between the supplier and the importer, the bills will be sent by the seller to the importer's bank or importer directly, and if the bills are directly sent by the importer, he will request the authorised dealer to make payment there under. The following guidelines are applicable:

- Bills should be received directly from the supplier's bank. However in some cases, Bills can be directly received from the supplier by the importer's bank (i) if the where value of good imported does not exceed USD 300,000, (ii) bills received from wholly owned subsidiaries of foreign companies from their principals. (iii) if the importer is a Status holder exporter or 100%EOU/Units in Special Economic Zones, PSU and Limited Companies (iv) Bills received by all limited companies (iv) Bills can be directly received from the supplier if Bank is satisfied.
- The bills received under collection by the Banks directly either from supplier's bank or the supplier are governed under Uniform Rules for Collection (URC 522) and hence should be guided by those rules. They should also ensure that the bills drawn under Letter of Credit are not sent under collection without being covered under URC 522.

Evidence of Import

7.43 It is necessary that the authorized dealer ensures that importer submits evidence of import to the Bank in a reasonable time. The evidence of import depends upon the type of import and such Bills of Entry (BEF) should be obtained and kept on record at least for a period of one year after audit of the branch is completed. In no case, the original BEF should be returned to the importer by the authorized dealer. The authorized dealer is required to acknowledge receipt of BEF.

As per the present guidelines BEF need not be submitted incase the import is up to an amount of USD 100,000. In all other cases, the BEF should be submitted to the authorized dealer within a period of three months from the date of remittance for import. The authorsied dealer may give an extension of three months for submission of such BEF and incase the same is not submitted even after the lapse of six months, the authorized dealer should report the same to RBI in the half-yearly return in June and December every year of all those pending BEFs over USD 100,000. Incase, the payment is made for Bills received on DA terms, the evidence of import should be submitted before making the payment for the imports.

It is advisable that the authorized dealer should verify the website, ICEGATE for genuineness of the BEF submitted by the importers.

Merchant Trade

7.44 In order to qualify a transaction under merchant trade both conditions to be satisfied are (i) goods acquired should not enter the Domestic Tariff Area and (ii)the state of the goods should not undergo any transformation.

In addition to that other conditions to be complied with under merchant trade are:

(i) goods to be imported/exported are permitted under FTP

(ii) both legs of trade are routed through same Bank

(iii) the entire transaction is completed within a period of 9 months

(iv) the transactions do not involve foreign exchange outlay for a period exceeding four months

(v) the commencement of Merchant Trade is the date of shipment / export leg receipt or import leg payment whichever is first

(vi) payment is received in time for the export leg first

(vii) Supplier's credit / buyer's credit is available to the extent advance remittance not received

(viii) advance remittance for import leg permitted

(ix) Letter of credit for the supplier permitted against confirmed export order

(x) payment for import may be allowed from EEFC balances

(xi) one to one matching of merchant trade should be ensured

(xii) the merchanting traders should be genuine trader of goods

(xiii) confirmed orders have to be received from their buyers.

The authorised dealer should ensure that (a) defaulting merchanting traders whose outstanding reach 5 % of their annual export earnings would be caution listed, (b) merchanting traders have to be genuine traders of goods and not mere financial intermediaries, (c) In case of Nepal and Bhutan are landlocked countries, Customs transit declarations have to be obtained.

Issue of Guarantee for Import of Services

7.45 Authorized dealers are permitted to issue guarantees for import of services at the request of import customers in favor of non-resident service provider for amounts not exceeding USD500,000.The guarantee is to secure a direct contractual liability arising out of contract between resident and non-resident. For issue of guarantee exceeding USD100,000 in respect of PS Company or Dept of GOI, MOF approval is required. If the guarantee is invoked, matter should be reported RBI.

7.46 Key points relating to various guidelines issued by RBI on Imports are narrated below:

(i) Import Trade is regulated by the DGFT under the Ministry of Commerce & Industry. While the physical merchandize concept is governed by the Foreign Trade Policy and implemented by the Customs Authorities, the Foreign exchange part is governed under the FEMA regulations and implemented by the RBI through the Authorized Dealers.

(ii) AD Banks should ensure that the imports into India are in conformity with the FTP in force (2009-14), FEMA rules 2000, adherence to the provisions of Income Tax Act, wherever applicable and directions by RBI from time to time.

(iii) AD Banks should ensure normal banking procedures, KYC guidelines & adhere to the provisions of the UCP while opening LCs for imports into India. Where specific regulations do not exist, AD Banks may be governed by normal trade practices in all their dealings.

(iv) Application for all Import payments exceeding USD 5,000/- towards Imports into India, should be supported by Form A1 and supported by documents(Import documents) to the satisfaction of the AD. AD Banks need not obtain any document including A-1 except a simple letter from the applicant containing the basic information, viz., the name and address of the applicant, name and address of the beneficiary, amount to be remitted, purpose of the remittance as long as the exchange being purchased is for a current account transaction.

(v) Remittances against Imports should be completed not later than six months from the date of shipment. However, AD Banks may permit settlement of import dues delayed due to disputes, financial difficulties, etc., beyond the 180 days subject to the condition that the AD is satisfied with the reasons put forth by the Importer.

(vi) Advance remittances towards Imports are allowed without any ceiling. However, if the amount exceeds USD 200,000 or its equivalent, such remittances should be supported by a bank guarantee. In cases where the Importer is unable to obtain the bank guarantee and the bank is satisfied about the track record and bonafides of the transaction, bank may permit such advance remittances without insisting for a bank guarantee subject to maximum amount of USD 5 Mn. Banks to put in place a policy approved by the Board of the bank in this regard.

(vii) The Importer is under obligation to submit the documentary evidence for having completed the Imports (Exchange Control Copy of the Bill of entry) within 6 months from the date of remittance in case of Advance Remittance. In respect of imports under D/A basis, the BOE should be submitted at the time of effecting the outward remittance and in case of D/P basis, the BOE has to be submitted within 3 months from the date of remittance. In case of default in submission of the evidence of Import, for amounts exceeding USD 1 Lac, AD should report such transactions to RBI in BEF Statement on half yearly basis.

(viii) For Imports with value of less than USD 1 Lac, Banks can insist for any other alternate document as documentary evidence for import in lieu of the Bill of Entry (subject to the Board approved policy of the Bank) that the goods have been imported along with reason for non-submission. the BOE.

(ix) In respect of import of non-physical Imports, a certificate from a Chartered Accountant that the software/data/drawing/design has been received by the Importer to be submitted to the AD.

(x) Import of gold on consignment basis by nominated agencies/banks is permissible only to meet the genuine needs of Exporters of gold jewellery. Exports. LCs opened by nominated Banks/Agencies for import of gold will be only on 100 % cash margin and should be on documents against payment basis (DP basis).

(xi) Imports can be handled in either of the following methods:

(a) Imports under Advance remittances-All advance remittances exceeding USD 2 Lac to be supported by a bank guarantee. If the Importer is unable to provide the guarantee, bank based on the relationship can waive guarantee for amounts upto USD 5 Mn. and BOE be submitted within 6 months from date of remittance.

(b) Letters of Credit-Letters of credit are a set of instructions given by the Importer and conveyed by the Importer's Banker to the Overseas Bank for onward transmission to the supplier with a commitment that payment under the LC will be made if the documents submitted are credit compliant. Opinion on the Overseas Supplier either through DNB or through a Banker is to be obtained. Before establishing the LC, credit processing and non-fund based limits are to be put in place. As per RBI guidelines, all import LCs are to be established for a tenor not exceeding 180 days from date of shipment (in case of procurement of raw materials) and 3 years in case of procurement of capital goods. All transactions under LCs are governed under extant provisions of UCP 600 established by ICC.

(c) Imports under Collection basis received by the Bank- Authorized dealers are to exercise due care while handling Import bills under Collection basis received on behalf of their Importers with reference to their line of business, financial standing, frequency of imports and track record to establish genuineness of imports. Satisfactory opinion report on the overseas supplier may be called for from the bankers, accredited rating agencies, etc., in support of the genuineness of the Import. Original documents received along with the Overseas Bank's covering letter to be thoroughly scrutinized to ensure adherence to the instructions contained therein. All transactions under collection are governed under the Uniform Rules for Collection – URC 522.

(d) Import Bills received directly by the Importer- AD Banks may make remittances where import bills have been received by the

Importers directly from the Overseas Supplier in respect of the following cases:

- Value of the import bill does not exceed USD 300,000 or equivalent where the Importer is a sole proprietor, partnership or an LLP.
- Import bills received by the WOS of Foreign Companies irrespective of the amount of the bill.
- Import bills received by status holder exporters, 100 % EOUs, Units in SEZs irrespective of the amount of the bill.
- Import bills received by PSUs irrespective of the amount of the bill.
- Import bills received by all limited companies (Public Limited, Deemed Public Limited and Private Limited Companies) irrespective of the amount of the bill.

Export of Goods and Services

7.47 The Foreign Exchange Management (Export of Goods and Services) Regulation, 2000, contains instructions regarding exports of goods and services and the same should be read with modifications made there under. Reserve Bank of India Master Direction no. RBI/FED/2015-16/11 FED Master Direction No. 16/2015-16 January 1, 2016 (updated upto 12.5.2016) consolidates all the directions issued there under.

Declaration of Export of Goods and Services

7.48 All exporters are required to declare the value of exports made under export declaration forms. There are three declaration forms, namely, Statutory Declaration Forms (SDF) issued by EDI (Export Data Interchange) ports which have been fully computerized. Export Declaration Forms (EDF) shall be issued by non – EDI ports. SOFTEX forms are used for software exports. PP (Post Parcel) form are used for export by post and VP/COD forms are used when goods are exported on Value Payable basis or Cash on Delivery basis.

Incase, the goods are exported in any of the situations, *viz.*:

(i) trade samples of goods and publicity material supplied free of payment

(ii) personal effects of travelers, whether accompanied or unaccompanied

(iii) goods or software whose value is not more than ₹ 25000

(iv) by way of gift of goods not more than one lakh rupees in value

(v) Aircrafts or aircraft engines and spare parts for overhauling and/or repairs abroad subject to their re-import into India after overhauling /repairs, within a period of six months from the date of their export

(vi) goods imported free of cost on re-export basis

(vii) goods not exceeding U.S.$ 1000 or its equivalent in value per transaction exported to Myanmar under the Barter Trade Agreement between the Central Government and the Government of Myanmar

(viii) The following goods which are permitted by the Development Commissioner of the Export Processing Zones or Free Trade Zones to be re-exported, namely, (a) imported Goods found defective, for the purpose of their replacement by the foreign suppliers/ collaborators, (b) goods imported from foreign suppliers/ collaborators on loan basis , (c) goods imported from foreign suppliers/collaborators free of cost, found surplus after production operations, (d) replacement goods exported free of charge in accordance with the provisions of Exim Policy in force.

Authorized Dealer may waive submission of Declaration forms if (a) the export of goods is free of cost, (b) for export promotion upto 2% of average annual exports during preceding three financial years, subject to a maximum amount of ₹ 5 lakhs for non-status holders and 10% for status holders whichever is higher. However, export of goods not involving any foreign exchange requires Reserve Bank of India approval.

Authorized Dealer may also approve submission of EDF for goods taken out for exhibition and participation in trade fairs subjects to (i) unsold exhibits may be sold outside the exhibitions, (b) unsold exhibits can also be gifted upto an value of USD 5000 per exporter, per exhibition/trade fair. The approval by authorised dealer is subject to (a) bill of entry produced within one month of re-import of unsold items, (b) the sale proceeds are repatriated immediately and (c) the method of disposal of items should be reported to him. All such transactions are subject to 100% by auditors.

Submission of Documents by Exporters

7.49 The exporter should submit all shipping documents (such as Bill of Lading, Insurance, invoice, etc.) along with declaration forms and other documents requested by the buyer to authorized dealer within 21 days from date of shipment. The documents may be submitted for negotiation if Letter of Credit has been established in favour of the exporter, and/ or for discounting of DA bills and purchase in case of DP bills. The authorized dealer should dispatch the documents to their overseas branches/ correspondents or as per LC instructions.

The exporters are permitted to send the documents and can be directly sent to consignees provided (i) Advance payment or an irrevocable letter of credit established for the full value and the sale contract provides dispatch of goods directly to them. (ii) The exporter is regular customer of the AD Bank. (iii) where the value of export does not exceed USD 1 Mn.

Status Holder exporter can directly dispatch the documents to the consignee provided the export proceeds are repatriated through AD named in EDF/SDF forms and the duplicate copy of EDF/SDF submitted within 21 days of shipment to AD.

Receipt of Payment for Exports

7.50 There is no restriction on invoicing of export contracts in INR or in freely convertible currency but export proceeds shall be realized in convertible currency only. The exporter must realize full value of the goods/software/ services should be realized within a stipulated period from the date of export. The stipulated period for receipt of export proceeds in all cases is maximum nine months and in case goods are exported to warehouses outside India, the period of realization is 15 months.

Banks can allow extension of time beyond nine months for a period of six months provided (i) the export transactions are not under investigation (ii) the exporter is unable to realize due to reasons beyond his control (iii) exporter submits a declaration that the same will be realized during extended period (iv) total outstanding of exporter does not exceed USD 1 Mn. or 10% of average realizations during preceding three years whichever is higher (v) all export bills outstanding beyond six months are subject to reporting under XOS statement (vi) extension may be permitted without any time limit if a suit has been filed by the exporter on consignee. Any further extension of time beyond the time allowed by Authorized Dealer, is subject to approval by Reserve Bank of India.

7.51 Payment should be received through authorized dealer by way of (1) Bank draft/personal cheque (2) to the debit of FCNR/NRE accounts of consignee held in India(3) International credit cards (4) Through OPGSPs – Online Payment Gateway Service Providers with maximum amount of USD 10,000 (5) FC/TC from buyer during his visit to India (6) In rupees/ ACU mechanism for Nepal and Bhutan (7)In precious metals, units set up in SEZs and EOUs equivalent to Jewellery exported.

Other conditions governing receipt of payment for exports are, incase the payments are from ACU countries they must settle in ACU Dollar or ACU Euro. In the case of Myanmar, the payment can be received in other currencies also. Third Party payments for exports are permitted. Payment should be received in the currency appropriate to the place of destination irrespective of residence of buyer.

Advance Receipts

7.52 Sometimes exporters may receive advance for the goods to be exported in future. In such cases, the export should be shipped within one year from receipt of advance payment. Incase the export agreement states that the export can take place beyond one year from the receipt of advance receipt, approval of Authorized Dealer is required. Incase agreements states so, exporter can pay interest on advance receipt at rate of interest not exceeding LIBOR + 100 bps. All the documents should be routed through the same authorized dealer through whom the advance has been received. Incase shipment does not take place within one year from the receipt of advance, RBI approval is required to refund the remittance.

7.53 Reserve Bank of India permits to receive advance payments for longer periods upto 10 years allowed subject to:

(i) Minimum of 3 years satisfactory track record of exporter.

(ii) Firm orders for export are in place.

(iii) Product pricing should be in consonance with prevailing prices.

(iv) The company has capacity to execute such long term orders.

(v) No Enforcement Directorate notices were issued to the company.

(v) Rate of interest payable on such advance remittances does not exceed LIBOR + 200 bps.

(vii) The documents should be routed through AD only.

(viii) Such advance above USD100 Mn should be reported to RBI.

(ix) Incase the exporter request for issuance of BG/SBLC in favour of the consignee who has given advance payment, should not be issued for more than for 2 years and then rolled over if requested by the exporter.

Write Off

7.54 The Authorized Dealers as well as exporters are permitted to write off unrealized export bills subject to limits specified by the Reserve Bank of India. Such write off is permitted only in the cases where, (i) the write off is outstanding more than one year, (ii) the overseas buyer has been declared as insolvent, (iii) the whereabouts of the overseas buyer are not available/ traceable, (iv) goods have either been destroyed or auctioned by the port authorities at the destination due to non-delivery of goods or non-payment of taxes, etc. (v) legal action is very expensive with reference to the amount to be recovered (vi) exporters surrenders proportionate incentives, if any, received from Government of India (duty drawbacks) or any other agencies (vii) submits a certificate from a Chartered Accountant certifying the export realizations during the preceding calendar year.

The exporter can "self-write-off" upto 5%, and Status holder exporters upto 10% and authorized dealer upto 10% of the total export proceeds realized during the previous calendar year.

Consignment Exports

7.55 When consignment exports are made, the account sales submitted by the exporter as received from his agents should be verified by the Authorised Dealer. In consignment exports, the freight for exports and marine insurance should be arranged before exports in India. Incase consign export relates to books, unsold books may be abandoned in foreign country and the value thereof should be shown as deduction from export proceeds of books.

Shipments Lost in Transit

7.56 When shipments from India for which payment has not been received either by negotiation of bills under letters of credit or otherwise are lost in transit, the AD Category – I bank must ensure that insurance claim is made as soon as the loss is known.

Netting of Export Receivables Against Import Payments

7.57 Requests received from exporters for netting off of export receivables against import payments for units located in SEZ are allowed by Authorized Dealer subject to (i) The 'netting off' of export receivables against import payments is in respect of the same Indian entity and the overseas buyer/ supplier (bilateral netting) and the netting may be done as on the date of balance sheet of the unit in SEZ (ii) The details of export of goods are documented in EDF (O) forms / DTR as the case may be while details of import of goods / services are recorded through A1 / A2 form as the case may be. The relative EDF will be treated as complete by the designated AD Category – I banks only after the entire proceeds are adjusted/ received(iii) Both the transactions of sale and purchase in 'R' - Returns under FET-ERS are reported separately (iv) The export/ import transactions with ACU countries are kept outside the arrangement (v) All the relevant documents are submitted to the concerned AD Category – I banks who should comply with all the regulatory requirements relating to the transactions.

Short Shipments and Shut out Shipments

7.58 When part of a shipment covered by an EDF already filed with Customs is short-shipped, the exporter must give notice of short-shipment to the Customs

Where a shipment has been entirely shut out and there is delay in making arrangements to re-ship, the exporter will give notice in duplicate to the Customs in the form and manner prescribed, attaching thereto the unused duplicate copy of EDF and the shipping bill.

Other Conditions in Exports

7.59 The following are other conditions in exports:

AD Category – I banks may allow payment of commission, either by remittance or by deduction from invoice value, on application submitted by the exporter.

AD Category – I banks, through whom the export proceeds were originally realized may consider requests for refund of export proceeds of goods exported from India and being re-imported into India on account of poor quality

Reduction in invoice value on account of prepayment of usance bills permitted upto proportionate interest on the unexpired period of usance calculated at interest rate LIBOR.

Reduction in invoice in other cases such as consignee demanding reduction before making the payment will be allowed by the Authorized Dealer upto a reduction not to exceed 25% of invoice value, the export commodities are subject to floor price, the exporter is not RBI caution list and incentives if received are surrendered. Change in buyer or consignee are also allowed by Authorized Dealer.

7.60 The Key points relating to various guidelines issued by RBI on Imports are narrated below:

(i) Export Trade is regulated by the DGFT under the Ministry of Commerce & Industry. While the physical merchandize concept is governed by the Foreign Trade Policy and implemented by the Customs Authorities, the Foreign exchange part is governed under the FEMA regulations and implemented by the RBI through the Authorized Dealers.

(ii) AD Banks should ensure that the Exports from India are in conformity with the FTP in force (2009-14), FEMA rules 2000 , adherence to the provisions of statutory guideline, wherever applicable & directions by RBI from time to time.

(iii) AD Banks should ensure normal banking procedures, KYC guidelines & adhere to the provisions of the UCP while advising/negotiating under LCs for Exports from India.

(iv) Where specific regulations do not exist, AD Banks may be governed by normal trade practices in all their dealings.

(v) All Export contracts and invoices shall be denominated either in freely convertible currency or in Indian rupees. However, exports realized in rupees should be through a freely convertible Vostro account of a non-resident Bank situated in any country, other than a member country of the ACU or Nepal or Bhutan.

(vi) Advance Remittances towards Exports - Exporters are permitted to receive Advance remittances towards Exports subject to the condition that the shipment of the goods should be effected within one year from the date of receipt of advance remittance. In case if the Exporter is unable to ship the goods within one year from the date of receipt of the remittance, any extension for shipment of the goods or for refunding the amount after one year requires prior approval from the Reserve Bank of India.

(vii) The amount representing full value of export value of goods shall be received through an AD Bank either in the form of Currency Notes, Bank Drafts, Pay Order, Banker's cheque, debit to FCNR/NRE account or through International Credit Cards of the Buyer. Exports realized in the form of Currency Notes tendered by the Overseas buyer during the personal visit to India can be accepted subject to the obtention of Currency Declaration Form (CDF) where the proceeds exceeds USD 5000 and after exercising due diligence as per AML guidelines.

(viii) All exports are to be supported by the original commercial/financial documents and accompanied by the Exchange Control Copy of the SDF/GR/SOFTEX/PP forms as the case may be.

(ix) It is obligatory on the part of the exporter to realize and repatriate the full value of goods or software to India within a period of 9 months from the date of export irrespective whether the Exporter is a status holder exporter or a 100 % EOU. However, in case of SEZs, there is no specific time period stipulated for realization and repatriation of the export proceeds.

(x) EEFC – Exchange Earners Foreign Currency Accounts may be opened by Exporters to park the exchange earnings realized on account of exports to the extent of entire 100 % of the proceeds. However, exporters are under obligation to convert the entire balances into rupees before the last day of the next calendar month after utilizing the balances for import payments, if any and against forward contracts booked against the balances.

(xi) General permission is available to all Exporters for opening of a temporary foreign currency accounts for participation in trade fairs and exhibitions abroad. Exporters are permitted to export goods for the purpose of exhibiting the same in overseas exhibitions, sale of goods in such exhibitions and repatriating the sale proceeds on conclusion of the exhibition. Exporters are also permitted to re-import the goods into the country after completion of the exhibition.

(xii) Unrealized Export Bills – Exporters have to follow-up with the overseas buyers for realization of the Export bills and repatriation of the proceeds thereon. However, due to the reasons beyond the control of the Exporter, if the goods exported are not realized within the due dates, the Exporters can get the export bills extended by submitting Form ETX along with the copies of documents evidencing follow-up with the overseas buyers. AD Banks will take on record the efforts put in by the Exporter and extend the due date for realization of the bills accordingly. Despite efforts by the Exporter for realization of the Exports, such bills can be written-off by the Exporter either by Self-write off or write off by the AD Bank in their books subject to adhering to the extant guidelines of RBI.

Foreign Contributions

7.61 Foreign contributions received in the country for person resident in India are governed by Foreign Contribution (Regulation) Act, 2010 read with Foreign Contribution (Regulation) Rules, 2011.

The Act is applicable to whole of India and also to foreign branches and subsidiaries of "Body Corporates registered in India". However, the act is not applicable to a company registered under Companies Act whose more than half of nominal capital is held by a foreign company or foreign source.

Foreign Source

7.62 Foreign source includes:

(i) The government of any foreign 'country' or 'territory' and its agency(s).

(ii) Any international agency(not being the United Nations or any of its specialized agencies).

(iii) a foreign company.

(iv) a corporation, not being a foreign company, incorporated in a foreign country or territory.

(v) a multi-national corporation as per clause (g).

(iv) A company within the meaning of the Companies Act, 1956 or Companies Act, 2013 and more than one-half of the nominal value of its share capital is held, either singly or in the aggregate by certain agencies mentioned in the Act.

(vi) A citizen of a foreign country.

Foreign Contribution

7.63 Foreign contribution (FC) means the donation, delivery or transfer made by any foreign source of any:

(i) Article, (not being an article given to a person for his personal use as a gift having market value of not more than 25,000)(present specified threshold);

(ii) Currency(includes Indian or foreign);

(iii) Security (per Section 2(h) of the SCRA, 1956 and includes any foreign security per Section 2(o) of the FEMA, 1999).

Cost in lieu of goods or services in the ordinary course of his business, trade or commerce shall not be treated as FC. However, infusion of foreign share capital in a company registered under section 25/Section 8 of the Companies is treated as FC.

Recipients of Foreign Contribution

Who can receive

7.64 Any Person who is having a definite cultural, economic, educational, religious or social programme (practically all NGO's having nationalist objects) can receive FC after getting registered under FCRA law or obtaining a prior permission from the Central Government. A private limited company may also seek prior permission/registration for receiving foreign funds in case they wish to do some charitable work.

Who cannot receive

7.65 In terms of Section 3 of the Act, foreign contribution shall not be accepted by the following persons:

(a) A candidate for election

(b) Correspondent, columnist, cartoonist, editor, owner, printer or publisher of a registered newspaper

(c) Judge, government servant or employee of any corporation or any other body controlled by Government

(d) Member of any legislature

(e) A political party or officer bearer thereof

(f) Organization of a political nature

(g) Association or Company engaged in production or broad cast of news

(h) Prohibited individuals or Associations

7.66 In terms of Section 4 of the Act, foreign contribution can be accepted by (i) Relative. (Any person receiving FC in excess of one lakh rupees or equivalent thereto in a financial year from any of his relatives shall inform the Central Government in Form FC-1 within thirty days from the date of receipt of such contribution (ii) Business receipt from official channel or as per FEMA, 1999 (iii) Scholarships(iv) Wages for employees working under him (v) As an agent of foreign of source for transactions with CG/SG.

No permission is required from Central Government if foreign contribution is accepted in form of (i) salary, wages, or other remuneration due to him (ii) By way of payment in the course of international trade or commerce (iii) As an agent of a foreign source (iv) By way of gift or presentation made to him as a member of any Indian delegation (v) By way of any scholarship, stipend, etc., (vi) Receipt of contribution from a relative not exceeding ₹ 8000 per annum (vii) Remittance received in ordinary course of business through official channels.

General Guidelines

7.67 The person accepting foreign contribution in the aforesaid manner need to register themselves with Ministry of Home Affairs and obtain a certificate of registration as specified under the Act. They should also get the accounts audited periodically and submit the reports to the Government. They must designate a Bank's Branch for receipt of contributions. A person receiving scholarship, stipend will intimate Central Government if such amount exceeds ₹ 36000 in an academic year. Donations accepted from an Indian who has acquired foreign citizenship, PIO/OCI card holders are treated as foreign contributions. However, contributions received from non-resident Indians need not be reported.

Role of Banks

7.68 Bank should send a report to Central Govt. within 30 days where an amount in excess of ₹one Crore has been received in the case of registered entities and in the case non registered entities, any amount received thereof. Bank should not allow any withdrawal or transfer or utilization of the FC amount till such time the Association produces documentary evidence from MHA permitting it to do so. FC that is returned to the donor (for want of registration or prior permission) without crediting in the account of the recipient need not be reported. Transfer of funds from one FCRA registered Association to another need to be reported.

PART III

Concurrent Audit Checklist and Core Banking System

Chapter 1
Concurrent Audit Checklist

1.1 For effective concurrent audit, it is essential that the audit planning and programme is detailed and pre-planned. Since the period during which the concurrent auditor is required to verify manifold items in the branch of the bank is limited, and transactions are numerous so rationing of the time of the concurrent auditor is a pre-condition to successful audit. The checklist is to be time oriented, with volume of transaction and vulnerability of the same being considered for ascertaining frequency of checking.

1.2 This checklist is based on suggested item of coverage as per RBI Circular "*Concurrent Audit System in Commercial Banks – Revision of RBI's Guidelines*" dated July 16, 2015. Unless there is a specific guideline by the bank, the suggestive checklist of various items with periodicity is given below:

(A) Cash

(i) Verifying daily cash transactions with particular reference to any abnormal receipts and payments.

(ii) Verify all cash transactions of ₹ 10 lakh and above reported in CTR.

(iii) Verify cash transactions of ₹50,000/- and above invariably indicate PAN no./Form 60.

(iv) Verify all expenses incurred by cash payment involving sizeable amount (i.e., ₹ 50,000 and above).

(v) Cash transactions through vouchers are properly authorized, authenticated and recorded in the books of accounts.

(vi) Daily vouchers are properly stitched and kept as per procedure.

(vii) No Bankers Cheque/DD/MT for ₹20,000/- and above is made in cash.

(viii) Verify whether surprise verification of cash by an officer other than the joint custodian is conducted. Carry out surprise checking of cash on hand and at ATM along with safekeeping and custody. '

Surprise check implies that the bank need not be informed by the auditor in advance about the date and timing of the physical verification sought to be undertaken. However, it is recommended that such surprise check should be done either before or after the banking hours so as not to cause any inconvenience. Further, the date on which such verification is carried out should be duly documented and unless the appointment letter so stipulates, the frequency of verification should be at the discretion of the auditor, depending upon his observation to the robustness of the system or otherwise.

(ix) Verify whether:

- Cash on hand as per the General Ledger matches with the physical cash on hand. Cash, for this purpose, will include domestic as well as foreign currency and coins. It includes imprest balances irrespective of where it is located.
- Foreign currency, if any, on hand matches with the Foreign Currencies register and General Ledger.
- Currency notes are properly sorted and bundled as per clean note policy of RBI. As per the RBI Guidelines, currency notes are not to be stapled/ stitched now.
- Based on the system of the bank for stuffing of cash and system of recording in ledger, verification of cash in ATM has to be done. If ATM is attached to the branch, then it requires same surprise checks as in the case of cash.

(x) Verify, at random, the entries pertaining to inward and outward cash remittances are adhered to the rules laid down in the matter of security, insurance, etc.

(xi) Verify cash movement records/register and comment on completeness of information captured, overwriting, if any, movement's records after closure of day end, transactions during the day, signature of cashier, etc.

(xii) Verify the trends of cash balance compared to cash retention limit. Report on whether the branch is holding cash balance beyond the cash retention limit, if procedure of the bank permits.

(xiii) Verifying whether cash remittance in Transit Account is reversed on the same day by debit to a proper head of account designated for it after receipt of proper acknowledgement/receipt where cash is remitted to a branch/bank.

(xiv) Verify whether register has been maintained for impounded counterfeit notes, and adequate reporting has been done as required by the RBI and respective bank's head office guidelines.

(xv) Verifying whether the branch remits its excess cash to link branch or Currency Chest.

(xvi) Verify whether Currency Chest transactions are properly accounted for and it's reporting to RBI is done promptly in case of delays/omission.

(xvii) Verifying whether keys to strong room, cash safe, and almirah for security printing books are in joint custody of the authorized officials.

(xviii) Verifying whether the branch remits its surplus balance with other banks regularly to the designated RBI center.

(xix) Verify the branch is permitted by the Head office/Regional office of the bank to retain foreign currency notes and have a specified retention limit for the purpose. Check whether the branch has not transgressed the retention limit fixed for the branch.

(xx) Verify that whether lost tokens have been displayed inside cashier's cabin.

Illustrative Checklist on Cash Management

			Remarks
(i)	Date of verification of cash.		
(ii)	Amount of cash held as on the date of verification.		
(iii)	Cash retention limit of the branch.		
(iv)	No. of days when cash retention limit exceeded during the month/ quarter and by which amount.		
(v)	Actual amount of cut/ soiled notes held.		
(vi)	The percentage of cut notes/soiled notes out of total cash held as on the date of surprise verification of cash.		
(vii)	Whether cut/ soiled notes have been kept separately.		
(viii)	Whether "Cash Discrepancy Register" has been maintained and excess/ shortages has		

	been reported to the higher authorities promptly.		
(ix)	Whether surprise verification of cash has been done by officer other than joint custodian officer/manager.		
(x)	Whether cash movement register has been maintained as per the guidelines.		
(xi)	Whether the branch is maintaining records/registers relating to inward/ outward cash remittances to currency chest properly and proper insurance cover has been obtained.		
(xii)	Whether currency chest transactions have been properly accounted and reported to RBI. (wherever applicable)		
(xiii)	Whether bait/ decoy money is kept separately in the bank.		

(B) Clearing

(i) Verify process of reconciliation with bank's account at Clearing House and review of old outstanding entries for reconciliation. Have any reasons/comments been recorded for the same? Whether the branch has taken adequate steps to have them resolved or squared up.

Whether it has been showing an increasing or decreasing trend in the clearing differences.

Verify whether account with the Main/Service Branch is reconciled every week.

(ii) Whether drawings are allowed against uncleared instruments. Whether such instruments are referred through prescribed register and passed by the Controlling Officer, if the drawings exceed the prescribed limit whether these are reported to the Controlling Authority. Examine whether interest was charged and report such omission for rectification.

(iii) Verify whether:

- Proper accounting of inward and outward clearing is being done on daily basis.
- If the branch is independently handling clearing, whether the clearing account is brought to nil every day, if not, comments to be noted down.
- Counter returns, inward and outward, if any, should be reported. In respect of cheques returned by other banks whether respective customer's account is debited.
- Safeguards are observed to ensure proper handling and custody including returned instruments.
- Service charges/incidental charges as prescribed are charged for the cheques returned in clearing.

(iv) Verifying whether credit for realized cheques are received promptly.

(v) Verifying entries which remain outstanding for more than 2days and checking for action taken for their disposal.

(C) Remittances/Bills for Collection – Inward and Outward

(i) Verify remittance of funds by way of TC/NEFT/ RTGS or any other mode in cash is exceeding the prescribed limit.

(ii) Verify documents of title (lorry receipts, railway receipts, etc.) obtained in favour of the bank and the concerned transporters are on the IBA approved list.

(iii) Verify whether proper accounting of inward and outward remittance transactions is done.

(iv) Outstanding balance in DP and other transit accounts pending payment beyond prescribed period.

(v) Verify whether prescribed service charges by way of exchange, commission, out of pocket expenses, interest, overdue interest in respect of all remittances, bills purchased and collection items are recovered.

(vi) Verify whether branch detains inward bills/ cheques/ collection item beyond the stipulated period.

DD/ TT/ MT

(i) Verify whether DDs/TTs/MTs of ₹ 50,000/- and above are issued through accounts and not against cash.

(ii) Verify physically the inward bills on hand and post parcels tally with records.

(iii) Verify whether returned bills are debited to "Past Due and Dishonored Bills" and followed up as per the guidelines.

(iv) Verify whether overdue bills are properly followed up/ non-payment notices are served.

(D) Deposits

(i) Verify adherence to KYC/AML guidelines in opening of fresh accounts and monitoring of transactions in such accounts and whether letter of thanks is being sent to new depositors.

(ii) Verify whether Form No. 60 where the depositor does not have PAN is held on record and the same are submitted as per laid down procedure.

(iii) Verify large term deposits received and repaid including checking of repayment of term deposit in cash beyond permissible limit.

(iv) Verify accounts opened and closed within a short span of time, i.e., accounts with quick mortality.

(v) Verify whether the receipt/ payment of term deposit beyond ₹ 20, 000/- is made only through current/savings bank account. or by A/c payee cheque.

(vi) Verify that inoperative/ dormant accounts are properly segregated and separate control thereon is exercised. Operation in dormant accounts are authenticated by the competent authority.

(vii) Verify value dated transactions.

(viii) Verify renewal procedure of term deposits. Whether deposits are auto renewed on due date if not closed.

(ix) Verify Interest paid on deposits during the quarter ended March, June, September and December, respectively as to whether the interest is correctly paid and maturity values correctly calculated at the prescribed rates as applicable to the category and term of deposits.

(x) Verify that deduction of tax at source from interest income on term deposits is made as per laid down procedure.

(xi) Verify procedure in place for settlement of claims of deceased customers and payment of TDRs against lost receipts and obtention of indemnities, etc.

(xii) Verify revival of dormant accounts and accounts with minimum activities.

(xiii) Examination of multiple credits to single accounts.

(xiv) Verify whether service charges for the return of cheques, issue of cheque books, carrying out standing instructions and minimum balance charges are levied as per prescribed norm.

(xv) Scrutiny of staff accounts to detect any abnormal transaction.

(xvi) Verifying that stop payment instructions are being recorded properly.

(xvii) Specific checks w.r.t debits in the inoperative accounts.

(xviii) Shifting of inoperative/dormant account to operative account is to be backed with KYC norms.

(xix) Cash withdrawal in dormant account should done personally by the account holder.

Account Opening Procedure

(i) These are filled in all respects and KYC norms are compiled with.

(ii) Xerox copies of all documents/ papers attached to the account opening forms are verified from the original and the bank official has passed necessary remarks with his signature on the Xerox copies for having verified the same for original.

(iii) Latest Photographs of the depositors/ all the authorized signatories are obtained and other requirements such as introduction, date of birth certificate in case of minors, nominations, etc. are compiled with.

(iv) Round stamp of the bank is affixed on photographs. Name of depositors is written on the reverse of the photographs.

(v) The bank officials have to verify the bonafide of the depositors and introducers, if required.

Debit Balance in Saving and Current Account

(i) Un-recovered debit balances in savings and current account that might have arisen due to various reasons are reported.

(ii) Interest on such debit balances is promptly recovered.

Issue of Cheque Books

(i) Proper procedures is followed for issuing of cheque books.

(ii) In case of Cheque books delivered to third person, necessary precautions as mentioned below are taken.

  (a) Authority letter bearing an attestation of signature of the person who is authorized to collect the cheque book, by the customer should be obtained.

  (b) Customer signature of said letter should be verified by the bank official.

  (c) Identity of the receiver of the Cheque book is established.

  (d) Cheque book receiver's signature is taken on the cheque book issued register.

  (e) Account holder is informed accordingly through SMS on mobile wherever possible.

(iii) Cheque books prepared but not delivered to the customer are kept safely under lock and key with the officer.

(iv) Guidelines as indicated in circulars issued from time to time regarding disposal of undelivered cheque books are followed.

(v) Wherever applicable, charges are received.

(vi) Cheque book when issued is immediately authorized in the system.

Nominations

(i) The appropriate nomination forms for deposits, lockers and safe custody are obtained and are serially numbered.

(ii) Nomination is entered in the system and authorized immediately.

(iii) The signature of the customer making the nomination is verified. Date of receipt of the nomination is marked on the nomination form/ account opening form.

(iv) Necessary remarks are noted on account opening forms, in the computer system and register.

(v) Screen print of nomination is attached to the application forms/ account opening form.

(vi) Acknowledgement of having received and registered the nomination is issued to the customer.

(vii) Nomination Register is maintained properly and posted upto date.

(viii) In case of settlement of claims to nominee, proper procedure is followed. KYC proofs as per the RBI guidelines of the nominee are obtained. Date of registration of nomination and the date of death of the depositor should be checked while setting the death claim to the nominee.

In case of request form the depositor the term deposit receipt wise nomination be accepted. However, while accepting the receipt wise nomination or account wise nomination in case of term deposit the following clause be inserted in the nomination form. "Nomination given in the nomination form for the receipt/s or term deposit account will be continued even after the renewal of the said term deposit/s unless the contrary fresh nomination instructions in the fresh nomination form are submitted to the bank."

Death Claim

(i) All death claims are settled within a fortnight.

(ii) The claim form is duly filled in.

(iii) NOC from all co-heirs, "Affidavit" on stamp paper regarding legal heirs duly notarized and signed by guarantors, etc. is obtained.

(iv) The claim has been sanctioned and documentation has been done accordingly.

(v) Procedures laid down for settlement for claim is followed properly. Indemnity bond is duly stamped and 50% of amount is kept in T.D.R. for a period of minimum two years.

(E) Treasury Operations

(i) Verify if branch has acted within HO instructions for purchase and sale of securities.

(ii) Periodic confirmation of derivative contracts with counterparties has been obtained.

(iii) Adherence to regulatory guidelines with respect to treasury deals/ structured deals.

(iv) Controls around deal modification/ cancellation/ deletion, wherever applicable.

(v) Cancellation of forward contracts and passing/ recovery of exchange gain/ loss.

(vi) Gaps and OPL maintained in different currencies vis-à-visprescribed limit for the same.

(vii) Reconciliation of Nostro and Vostro accounts-balances in Nostro accounts in different foreign currencies are within the limits prescribed by the bank.

(viii) Collection of underlying documents for derivative and forward contracts, delays, if any.

(ix) Instances of booking and cancellation of forward contracts with the same counterparty within a span of couple of days or a few days.

(x) Sample check some of the deals and comment on the correctness of computation.

(xi) Checking of application money, reconciliation of SGL account, compliance to RBI norms.

(xii) Checking of custody of unused BR forms and their utilization in terms of Master Circular on Prudential Norms on Classification, Valuation and Operations of Investment Portfolio by banks.

(xiii) To ensure that the treasury operations of the bank have been conducted in accordance with the instructions issued by the RBI from time to time.

(F) Advances

(i) Verify fresh loans and advances (including staff advances) have been sanctioned properly and in accordance with delegated authority.

(ii) Whether appraisal of the proposals sanctioned are proper and disposed within the prescribed time norms with emphasis on credit sanction efficacy at branch level.

(iii) Verify that disbursals are allowed against proper sanction, within sanctioned limits and drawing power.

(iv) Whether all conditions of sanction have been complied with and to ensure "Certificate of Compliance" if any of sanction terms are submitted to respective sanctioning authority.

(v) Whether Legal Vetting Certificate, wherever prescribed had been taken.

(vi) Verify reporting of instances of exceeding delegated points to the controlling/head office by the branch have been confirmed or ratified by the competent authority.

(vii) Verify whether securities and documents have been received as applicable to particular loan.

(viii) Verify operations allowed in advances accounts:

- Whether they are within the sanctioned limits of drawing power (worked out as per the latest statements and prescribed margin).
- Whether operations in the accounts reveal any unhealthy features, such as, heavy withdrawals in cash suggestive of diversion of funds for purposes other than the declared business of the borrowers, diversion to sister/ associate concerns, diversion of funds to other banks, kite flying, etc., or any other sticky/ unhealthy tendencies which may jeopardize the interest of the bank.

(ix) Verify whether in the case of all advances against hypothecation of goods/ stock/ book debts, etc. [CC(hyp), PCL (hyp), etc.]

- Periodical statements declaring stock/ debtors, etc. as the case may be, are received from the borrowers within the stipulated due dates; whether the statements are properly scrutinized by the branch officials.

- Reports of verification of securities by third parties are received timely and whether penal interest is being charged for delayed submission. Reports are as per requirements of respective banks.

(x) Verify whether book debt statement certified by a chartered accountant, as stipulated by the bank, has been obtained.

(xi) Verify whether creditors have been reduced while calculating DP.

(xii) Verify whether monthly updating of drawing power in the computer system on the basis of stock statements/book debt statement/ other financial data has been received from the borrowers.

(xiii) Verify whether securities have been properly charged/ registered and valued by competent person. Whether the same has been entered in the bank's system.[Refer RBI Guideline # F. (vi)]

(xiv) Verify value dated entries passed in advances accounts.

(xv) Verify whether post disbursement, supervision and follow-up is proper, such as, timely receipt of stock and book debts statement, QIS Data, analysis of financial data submitted by borrower, verification of securities by third parties, renewal of limits, insurance, etc.

(xvi) Whether Select Operational Data and Management Report/HMR, where applicable, in respect of big borrowers have been received promptly as prescribed in the sanctioned letter.

(xvii) Verify whether the branch has charged lead bank charges in respect of advances under consortium norms.

(xviii) Verify master data relating to limit, rate of interest, EMI, moratorium period details have been correctly entered and updated/ modified in the system.

(xix) Verify compliance of prudential norms on income recognition, asset classification and provisioning pertaining to advances.

(xx) Recovery in compromise cases is in accordance with the terms and conditions of the compromise agreement.

(xxi) Verify whether bills are purchased as per terms of sanction and proper margin is maintained as per sanction.

(xxii) Verify whether pre-sanction verification is done before sanction of BP limits.

(xxiii) Verify and report clean bills/ cheques purchased, if in the nature of accommodation bills. Ensure that local cheques are not purchased unless specifically permitted.

(xxiv) Verify proper follow-up of overdue bills purchased/discounted/negotiated.

(xxv) Verify (on sample basis) by surprise goods pledged to the bank to ensure that keys of the godown are held in dual custody, goods pledged to the bank tally with the record maintained in the Godown Register and the invoices both for quantity and value.

(xxvi) Verify if godown inspection is being conducted periodically and is properly recorded and reports thereof raised/ submitted.

(xxvii) Verify if stock statements (indicating the location) are being received at stipulated intervals, the statements are properly scrutinized, drawing power is correctly calculated, DP Register is maintained and drawings/availments in the account so regulated. If the stock is with third party, then obtain NOC from the third party and their bankers.

(xxviii) Verify if all assets charged to the bank are fully insured against all risks and Due Date Diary for insurance policies is maintained, covering all stock locations.

(xxix) Verify whether NSCs/KVPs against which advance has been allowed have been pledged in favour of the bank and the said lien is marked by the concerned Post Office. Relevant securities are sent to and received back by the registered post/speed post unless specified otherwise. The envelope for NSCs/KVPs is held on record.

(xxx) In case of advance against LIC policy, the amount should be allowed only against surrender value and LIC policy in original with assignment is held on record.

(xxxi) In respect of consortium advances, the concurrent auditor should conduct inspection as per decision of the consortium where the turn comes to the particular branch for inspection.

(xxxii) In respect of sick and viable units, report on the implementation of a nursing package, if any, progress in preparing a rehabilitation plan, whether the progress report are received and studied, and comment on the current health of the unit. Whether the matter was considered by BIFR, if so, status of references to BIFR. List out weak areas in the unit to be strengthened. Whether functioning of the unit is in accord with earlier projections submitted to the bank and approved.

(xxxiii) To check review and renewal of loans.

(xxxiv) To check recovery of processing charges.

(G) LC/BG

(i) Verify whether issue of LCs/ BGs are in line with the extant guidelines.

(ii) Verify whether appropriate commission is collected in respect of fresh/renewed LCs/ BGs.

(iii) Whether securities including deposits are linked in CBS to LCs/ BGs.

(iv) Verify whether issue of LCs/ BGs are reported timely to Zonal Office/Regional Office.

(v) Verify whether LC/ BG is issued/amended as per approved format/model, if any, and whether standard limitation clause is incorporated. Whether counter indemnity obtained as prescribed.

(vi) Verify whether there is any deviation from the terms of sanction in regard to margin, security, purpose, period, beneficiary, collection of charges, commission, fees, etc.

(vii) Whether the branch has paid/ met any guarantee obligation under bank guarantee issued by it; whether payment is made to the debit of party's account on due date without creating overdraft/ debiting suspense, in case of deferred payment guarantee.

(viii) Whether bills paid on the previous day under LC are strictly according to terms of the LC; whether reimbursements have been obtained promptly.

(ix) Whether correct entries are passed on issued/ expired/ cancelled Bank Guarantees/ Letter of Credit issued/ expired/ cancelled.

(x) Whether there are any bank guarantees continuing even after their period of expiry; if so ascertain the reasons therefore, and whether steps are taken by the branch to close them as per stipulated procedure.

(xi) Verify the limits/accounts falling due for review, renewal and the action taken by the branch on it.

(xii) Verify whether Due Date, Diary of review/ renewal is maintained and required follow-up made on those dates.

(xiii) Verify whether the LCs are closed in the system after full utilization or expiry of the LCs.

(xiv) While opening LC please verify whether credit report of the beneficiary from approved agency has been obtained.

(H) Foreign Exchange Transactions

(i) Verify that LC and Bank Guarantee are issued as per terms of sanction and charges are recovered as per FEDAI Rules/ HO Guidelines.

(ii) Verify whether branch is adhering to Head Office guidelines issued under delegated discretionary framework of FEDAI.

(iii) Verify whether all the terms and conditions in the LCs are FEMA compliant, i.e., adhering to the FEMA regulations relating to exports.

(iv) Verify that packing credit released is backed by LC or confirmed export order.

(v) Verify whether the drawing power is ascertained before disbursement of Packing Credit (applicable to running account facility).

(vi) Verify whether the PC is liquidated by either a post shipment finance or from the balances in the EEFC accounts.

(vii) Verify ECGC cover is available and the ECGC terms are complied with. In case of running packing credit accounts, whether RBI guidelines are complied with.

(viii) Verify submission of statutory returns on export/ import transactions, like, BEF (if applicable) statements, XOS (if applicable), write off of export bills, R-return, etc. Follow up of outstanding export bills and exchange control copy of bill of entry.

(ix) Verify whether the branch is following up with the Importers for non-submission of the BOEs, and whether proper records of such follow up are kept at the branch level.

(x) Verify whether branches are following up with the exporters for submission of documents where advance remittances towards exports have been received and whether proper records of such follow up are kept at the branch level.

(xi) Irregularities in opening of new accounts and operation in NRE,FCNR, EEFC, NRO, etc., and debits/credits entries permissible under the rules.

(xii) Verify whether operations in FCRA accounts are as permitted by MHA and FCRA guidelines.

(xiii) To monitor whether FEDAI rules have been observed in the extension and cancellation of forward contract. Whether competent authority scrutinizes them and the necessary charges, including delivery charges, have been recovered.

(xiv) Verify whether in case of negotiation/purchase/discounting of Bills under LC, prescribed procedure like, verification of signatures of the Issuing Bank have been followed and scrutiny report issued. Verify booking, utilization, extension and cancellation of forward contracts.

(xv) Verify reconciliation of NOSTRO and VOSTRO accounts and verify for random dates that balances in NOSTRO accounts are within the limit prescribed by the bank.

(xvi) Verify whether the NOSTRO credits are processed without delay and credit is given to the customer's account on time.

(xvii) Verify correctness of charges levied on foreign inward/outward remittances.

(xviii) Monitor timely/ proper submission of claims to ECGC.

(xix) Adherence to the guidelines issued by RBI/HO about Dealing Room Operations*.

(xx) Verify that the title to goods is in the name of the bank.

(xxi) All FCNR receipts are issued by the branch against consideration, i.e., only after receipt of funds. High value deposits need special attention.

(xxii) Whether rates quoted/applied by the branch on various types of purchase/sale transactions are correct.

(xxiii) Verify that over bought/oversold position maintained in different currencies is reasonable taking into account foreign exchange operations as well as the extent up to which permission has been given to the branch by the International Division of Head Office for such positions**.

(xxiv) Payment of ECGC premium/submission of required statements to ECGC for pre-shipment/post-shipment.

(xxv) Verification of bill of entry and maintenance of proper records for it.

(xxvi) In respect of overdue packing credits, confirm whether they are Firm Order /LCs. Whether report to ECGC is made and premium is paid, whether RBI's approval is sought in case beyond power of authorized dealer.

(xxvii) Whether commercial rate of interest since first day of release is charged for overdue packing credits and those adjusted otherwise than by export bills.

(xxviii) Verify whether the bills negotiated/discounted/purchased are within the delegated powers of the branch.

(xxix) Whether export bill negotiated/purchased/discounted is not realized on due date (in case of demand bills within Normal Transit Period and incase of usance bills on the notional due date), exporter's foreign exchange liability should be converted into rupee liability as per policy of individual bank from the notional due date at prevailing TT Selling Rate.

(xxx) In case, additional facility is given to exporter in the form of Packing Credit in Foreign Currency (PCFC) or in the form of Rediscounting of Export Bills Abroad (EBRD) whether conditions applicable to these are complied with.

(xxxi) While opening LC please verify whether credit report of the beneficiary from approved agency has been obtained.

(xxxii) Verify whether there are any instances where the Non-resident Indian maintains a resident account with the bank. (It can be verified by taking a report on Cust-ID level of the customer).

(xxxiii) Verify whether the branch is adhering to Foreign Contribution Regulation Rules, 2010.

(xxxiv) Verify whether the guidelines relating to Interest subvention scheme/Interest equalization scheme is adhered to in full.

*Applicable only to Category "A" branches.

** Applicable to both Category "A"& "B" branches.

(I) House Keeping

(i) Verify Exceptional Transaction Reports are generated and verified by the branch staff as prescribed. Critically analyze the contents of the report also.

(ii) Review of all balance sheet heads and outstanding entries in accounts, e.g., suspense, sundry and inter-bank accounts. Review of follow up of entries pending for reversal.

(iii) Scrutiny of daily vouchers with more emphasis on high value transactions and debit entries in suspense account.

(iv) Verify debits in accounts where signatures are pending for scanning.

(v) Verify whether records related to KYC/vouchers and other critical areas are sent to specific places like, archival center, record room as per stipulated periodicity.

(vi) Verify adherence to KYC/AML guidelines in opening fresh account and subsequent modifications of records and monitoring of transaction.

(vii) Listing out the Book/Register/Ledger/General Ledger Account heads not checked and/or not balanced. Latest balances taken, amount of balances short/excess, balances differences freeze out, if any, with remarks and actions taken.

(viii) Whether the branch regularly follows up the outstanding entries for early elimination. Whether any non-prescribed transactions/ extraneous entries in violation of guidelines have been routed through the Sundry Debtors account.

(ix) Suspense accounts (Sundry debtors) at the branch do not contain any extraneous entries pertaining to clearing cheques returned as it may be an attempt to conceal TOD. Special attention need be given at the end of

June, September, December, March for entries of inward clearing cheques parked for the purpose of inflating deposit figures.

Note: Test check a few entries for ₹ 10,000/- and above as to whether they relate to authorized transactions and authenticated by the branch head. Verify entries in suspense account for entire period.

(J) Merchant Banking Business

(i) Verify, where the branch acts as a collecting branch for issue business, the instructions given by the controlling branch are properly followed.

(ii) Verify whether daily collection position is advised to the controlling branch.

(iii) Verify the funds are transferred to short deposit account as instructed and particulars of individual short deposits are advised to the controlling branch regularly.

(iv) Verify final certificates are submitted properly and in time to the controlling branch.

(v) Verify that the entire funds collected are remitted to the controlling branch, inclusive of amounts matured, the short deposits and interest thereon giving complete details of break-up of aggregate amount.

(vi) Verify that the branch does not accept applications from investors after the stipulated closing date of the issue.

(vii) Verify where the branch acts as a controlling branch, the terms and conditions on which the branch has accepted the role of banker to the issue are complied with.

(viii) Verify that there is no delay in the issue of final certificates by the branch in its capacity as controlling branch.

(ix) Verify whether the prescribed preventive vigilance measures are duly observed by the branch.

(x) Verify where data entry or data processing work is entrusted to outside agencies, the competent authority duly approves these and the prescribed stamped indemnity has been obtained from such agencies.

(xi) Verify that it is ensured that dividend interest warrants/refund payment accounts of companies are funded prior to dispatch of the relative warrants by the companies and there is no misuse of the facility. Verify whether deviations, if any, have been made after obtaining the approval of the competent authority.

(xii) Verify that branch is correctly recovering of the commission/ fees and out-of-packet expenses from the concerned companies. Verify whether the competent authority has duly authorized any waiver or reduction of such charges.

(xiii) Verify claims for reimbursement of amounts of paid warrants received from paying branches are processed and debited to the concerned company's account promptly. Cases of inordinate delays in raising debits, if any, are mentioned.

(xiv) Verify whether charge on security has been created, wherever debenture trustee activity is undertaken by bank.

(K) Credit Card/Debit Card

(i) Verify that the application for the issue of credit card has been properly examined and record of issue of the same has been maintained.

(ii) Ensure that the charge-slip is examined to verify that it does not cover any picked-up card.

(iii) Ensure that the overdraft/ debits arising out of the use of credit cards are promptly recovered and higher authorities are invariably informed about the same.

(iv) Verify that the bank maintains a proper record of picked-up cards.

(v) Verify that undelivered credit cards are properly kept as security items and followed up with credit card department for further instructions.

(vi) Carry physical verification of ATM cards, debit cards, credit cards, passwords and PINS, control over issue and delivery, safe keeping and custody at all the locations. Report loss of any such items.

(L) Accounts with Other Bank

(i) Verify whether large idle balances are maintained with banks and if so, the amount and for what period at a stretch. Ensuring that the branch obtains full particulars of debits/credits in the account and entries are promptly recorded.

(ii) Verify and review balance confirmation and reconciliation for accounts in other banks, periodically as specified by the bank.

(M) Documentation

(i) Whether documents register, or any other similar record; if prescribed by the bank is maintained up-to-date. Entries are made in this register and found in order. If there is any omission, it should be reported.

(ii) Verify that all documents have been correctly executed in the latest revised prints of prescribed formats and properly stamped, wherever necessary, in terms of Stamp Act of the respective state, as per manual on documentation and as per circulars on the subject.

(iii) Where immovable properties are held as security by way of deposit of title deeds, verify title deeds register to see whether narration is written for additional limits and all formalities have been complied with and verify:

- that original title deeds are with the bank.
- legal vetting by the banks empanelled advocate has been carried out with an unconditional confirmation by the advocate that a valid equitable mortgage can be created.
- certified copy of chain of property with confirmation of the advocate having verified documents available in the municipal records for the number of years as prescribed by the banks.

(iv) Whether legal opinion and valuation by the bank's advocate/ valuer are obtained for all the mortgaged properties, and the latest Encumbrance Certificate as well as tax receipts is obtained up-to-date and valuation has been carried by the specified value as prescribed by the bank.

(v) Proper recording of extension of the charge of equitable mortgage for enhanced credit facilities and/ or other credit facilities has been complied with.

(vi) Verification with CERSAI records should be carried out before disbursement/creation of mortgage as applicable.

(vii) Verify whether signature of executants/property owners are available on letter of confirmation of creation for having created equitable mortgage on the record.

(viii) In the case of company/ limited liability partnership (to the extent applicable):

- Whether copy of resolution passed by the company's board is on record for availing the credit facilities from the bank.
- Whether the authorized signatories as mentioned in the board resolution have executed the documents.
- Whether common seal, if applicable, has been affixed on the relevant document.
- Whether bank's charge or modification thereof has been registered with the Registrar of Companies(by filing Form 8).
- Whether search report of company's earlier charge has been made.

(ix) Check classification of advances as per RBI's Prudential Norms.

(x) Wherever registered mortgage has been prescribed in terms of sanction, verify whether the same has been carried out properly.

(N) Renewal of Documents and Time Barred Accounts

(i) Verify limits/accounts falling due for review, renewal and action by the branch. Verify whether due date diary of review/renewal has been maintained and required follow up has been done on those dates.

(ii) Whether the debts/decrees are time barred. Action takento be commented upon.

(O) Bills Purchased/Discounted/LCBR (Import LC Documents)

(i) Verify whether bills purchased/ discounted are genuine trade bills accompanied by lorry receipts of IBA approved transport operators; or railway receipts or airway bills or bills of lading or any other approved mode of transportation, and prima facie no unhealthy features are observed in the transaction.

(ii) Verify whether any bills purchased/ discounted/ negotiated were returned unpaid and if so, whether they are properly dealt with and reimbursement has been obtained promptly including interest at applicable rate. If the reimbursement is not prompt, verify whether the same has been reported.

(In case there are frequent returning of bills for huge amounts pertaining to a borrower, verify the reasons thereof and whether such cases have been reported to the concerned sanctioning authority)

(iii) Verify the bank guidelines for bills once discounted and returned are not again discounted.

(iv) Verify that there is proper follow-up of overdue bills.

(v) Verify the realization advices adjusted in respect of outward bills realized (purchased/ discounted/ negotiated/collectedfor large amounts (say ₹10.00 lakh and above) as to genuineness of the adjustments.

(vi) Whether in the case of bills purchased/ discounted/ negotiated the liability is within the limits. Verify that such transactions with allied/sister concerns are allowed if specifically permitted.

(vii) Whether any excess drawings/ bills beyond the sanctioned limits/ drawing power are allowed and if so, whether the branch has forwarded ratification/ confirmation of the concerned sanctioning authority. Whether such excesses are under the authorization of the branch head and properly recorded in the prescribed register and reported to the appropriate authorities.

(viii) Verify whether there are any bills purchased/ discounted/ negotiated outstanding beyond a reasonable period/ beyond due date and observation of any unusual/ unhealthy feature; ascertain reasons for overdue and whether reported to the concerned authorities in the prescribed manner.

(ix) In respect of bills purchased/discounted/negotiated, whether goods are appropriately protected with insurance.

(x) Whether credit report on drawers in respect of bills and drawers in respect of cheques is obtained?

(xi) Whether LC documents were verified with LC terms? Whether LC bill was rejected by the importer for any reason of non-compliance with LC terms, etc.

(xii) Whether cheque/bills are dispatched promptly, at least on the next day.

(xiii) Whether interest/commission, as prescribed, has been collected?

(xiv) Does the branch ensure dispatch of returned cheques by registered post if they are not collected immediately? Incase any deviation is noticed, please give full details.

(xv) For supply bills, verify whether the branch ascertained the genuineness of the underlying contract and power of attorney registered in the bank's favor.

(xvi) What is the system of follow up for the recovery of returned bills? How long have they been kept pending?

(xvii) Are the goods covered generally traded items/dealt with by the borrower?

(xviii) Verify in respect of all overdue and returned bills (including bills under LC), action taken by the branch is as per the guidelines.

(xix) In respect of export bills purchased/discounted, expressed in foreign currency, whether overdue bills were promptly converted into rupees under report to the central office.

(xx) Whether packing credit was adjusted out of export bills purchased.

(xxi) Comment on cases where payment has been received under reserve.

(xxii) ECGC policy as applicable is held and buyer wise limit is complied with.

(xxiii) Whether appropriate margin has been maintained as per sanction terms.

(xxiv) Whether the turnover in bills limit reflects the true position of sales as evidenced from financial statements. Large variation should be commented.

(xxv) In case of foreign bills purchased/ discounted for export on FOB and C&F terms, whether the contingency risks policy is as per Head Office instructions.

(P) Cash Credit Including Temporary Overdrafts

(i) Verify whether the branch has identified and classified the advance in accordance with the guidelines of the RBI and the Head Office.

(ii) Report individually on accounts in which there are irregularities due to:

(a) Excess drawing over drawing power

- (b) Excess drawing over limit
- (c) Deficiency in documentation
- (d) Operations unsatisfactory/no operation
- (e) Drawings against unclear effects
- (f) Non-recovery/absorption of interest
- (g) Not covered by sanction
- (h) Unreported excesses
- (i) Drawings not reflected by QIS where applicable
- (j) Account not brought to credit as per sanction terms

(iii) Verify whether passing of cheque is duly authorized through Cheques Referred Register, and whether there are irregularities as mentioned above.

(iv) Whether excess over the limit/drawing power is covered by adequate security and prescribed margin is maintained.

(v) Whether sundry creditors are reported in stock statement are deducted to calculate drawing power against paid stocks.

(vi) Whether any spurt in inventory is noticed and verified for the source of funds.

(vii) Whether norms for inventory and receivable, wherever applicable is being monitored.

(viii) Whether appropriate action has been taken where the non-submission of stock statement persists for more than two months.

(ix) QMR/HMR are studied critically and date are entered in a register for follow-up at the time of annual review. Whether variations from projections are analyzed and considered realistic, based on past performance and environmental outlook. A concurrent auditor needs to verify the adequacy/enforceability of insurance or insurable assets with appropriate risks, location, etc. The concurrent auditor needs to indicate cases where a delay in the recovery of interest has been noticed. *Ad hoc* facilities allowed to continue beyond the stipulated period mentioned in sanction, also need to be highlighted. Excess beyond the *ad hoc* limit without report/confirmation and allowed to continue without recovery to be pointed out.

(x) In case, specifically mentioned by the bank, the concurrent auditor should conduct inspection ofunits/godown/fixed assets/stocks under pledge and hypothecation in such a way that all the accounts are inspected as terms of appointment letter at least once in every six months. Stock inspection report should be in the prescribed format of the bank for this purpose.

(Q) Advances under Consortium Arrangement

(i) Verify whether consortium meetings are held and minutes of meeting are prepared. Verify whether minutes of the meeting are communicated to all consortium members. The branch keeps the controlling office informed of all the meetings and deliberations.

(ii) A confirmation from the lead bank that original documents are held by the bank on behalf of all the member banks. Securities are created by them on behalf of all member banks and equitable mortgages are held by them on behalf of all banks.

(iii) Joint inspections of the unit/stock are carried out as per joint lender's agreement. Verify that the irregularities in the inspection report are promptly attended to.

(iv) Verify that pro-rata business, including non-fund based business, is transacted through the bank.

(R) Refinance Management (NABARD/SIDBI/Exim Bank)

(i) Whether all eligible term loans disbursed has been identified and reported to competent authority without delay.

(ii) Whether the commercial rate of interest has been charged till the date of refinance.

(iii) Whether the branch has ensured that the claim is in order.

(iv) Whether the branch has been kept informed by the principal account holder and those liable under the counter guarantee.

(v) In respect of Deferred Payment Guarantee, whether payment is made to the debit of party's account on due date without creating overdraft/debiting suspense.

(S) Other Assets/Sundry Creditors/Accounts

(i) All Pension Payment Order (PPO's) are properly numbered and recorded.

(ii) Records at branch for pension payment order are up to date. Verify whether any excess pension payment is outstanding in branch for recovery.

(iii) Verify whether link branch (if applicable) is sending pension payment scroll to RBI/SBI well in time for reimbursement.

(iv) Verify whether, every November, Life Certificate has been obtained in case of all PPO's.

(v) In case of undisbursed pension, check that the amount has been promptly returned.

(vi) Whether TDS has been deducted as per extant rules.

(vii) Whether turnover commission is recovered by the link branch and distributed amongst branches.

(viii) Whether reimbursement are in arrears.

(ix) For collection of taxes, PPF A/c, etc. whether funds received are immediately remitted to link branch.

(x) Ensure at least 30% scrutiny of transactions relating to the payment of pension has been done.

(xi) Whether the prescribed certificates - Life, Re-employment, Re-marriage, etc. has been obtained, wherever required, in all pension accounts.

(T) Others – Verify

(i) Compliance of provisions relating to tax deducted at source, service tax, trade tax, other duties and tax.

(ii) Physical verification of inventory, control over issue of inventory, safe keeping and custody of security forms. Report any loss of such items.

(iii) Physical verification of other deliverable items, control over issue, safe keeping and custody.

(iv) Physical verification of gold coins, control over issue, safe keeping and custody. Checking of gold sale transactions.

(v) Custody and movement of branch keys.

(vi) Locker keys and locker operations – linking of FDR as security for locker/ operation of locker/ inoperative lockers/ nomination/ other issue.

(vii) Safe custody of branch documents like, death claim cases, issuance of duplicate DD/PO/FDR, checking of indemnities, etc., and verification of documents executed during the period under audit.

(viii) Reporting of frauds.

General Banking- Income Tax/Service Tax/Other Tax Related Issues

(i) Verify the transactions where 'PAN' is mandatorily to be submitted under Rule 114 B of the Income Tax Rules,1962. In case where such person does not have 'PAN' he shall make a declaration in Form 60, giving therein the particulars of such transactions. The transactions are:

(a) A time deposit with banking company for an amount exceeding ₹ 50,000/- or aggregating to more than ₹ 5 lakh during a financial year.

(b) Opening an account other than as mentioned in (i) above and a Basic Saving Bank Account.

(c) Making an application to any banking company for issue of credits or debits cards.

(d) Deposit with a banking company of cash exceeding ₹ 50,000/- during any one day.

(e) Purchase of bank drafts or pay orders or banker's cheques from a banking company where payment was made in cash for an amount exceeding ₹ 50,000/- during any day.

(f) Payment against purchase of any foreign currency at any time, in cash, of an amount exceeding ₹ 50,000/-

(g) Payment against sale/purchase of goods/services for amount exceeding ₹ 2 lakh per transaction.

(ii) Verify whether banks which have received any declaration in Form No. 60,as stated in para 'a' above, on or after 01-01-2016 in relation to any of above transactions referred to in Rule 114 B of Income Tax Rules,1962 shall:

(a) retain such Form 60 for a period of 6 years from end of financial year in which transaction was undertaken, and

(b) furnish a statement in Form No. 61 to the Director of Income tax (Intelligence and Criminal Investigation) or the Joint Director of Income Tax (Intelligence and Criminal Investigation) through online submission of electronic data to a server designated for this purpose and obtain an acknowledgement number thereof.

(c) Such filing of Form No. 61 is to be made within prescribed time, i.e., upto 31st October for declarations received upto 30th September and upto 30th April for declarations received from 1st October to 31st March.

(iii) Verifying the obtention of PAN and updation of the same in computer.

(iv) Verify whether fixed deposit of ₹ 20,000/- or more has not been repaid in cash. This is in contravention of provisions of Section 269T of Income Tax Act,1961. In case repayment is made by any branch of a banking company, such repayment may also be made by crediting the amount of such loan or deposits to the saving bank account or current account with such branch.

(v) Verify whether the compliance of section 206AA of Income Tax Act,1961 has been made with regards to furnishing of 'PAN'.

(vi) Verify the compliance of issues relating to TDS on salary, pension, disbursement, rent, commission, interest, payment to contractors, payment of fees to professional/technical person, etc. in respect of:

- Deduction of TDS at correct rate.
- Deposit of TDS within time.
- Filing the TDS return in time and as per procedure prescribed.
- Issue of TDS certificates.
- Receipt of 15G and 15H and entry in system.
- Filing of Form 15G/15H with department as per new procedure.

(vii) Ensure whether Form 15CA and 15CB has been obtained for outward foreign remittance and filing of details of these forms in Form 15CC as per Rules 37BB which states that banks shall furnish a quarterly statement for each quarter of the financial year in Form No. 15CC as per procedure given in Rule 37BB.

(viii) Ensure that no payment has been made exceeding ₹ 20,000/- against an expenditure otherwise than through an Account Payee Cheque or Account Payee Bank Draft to comply with provisions of Section 40 A(3) of the Income Tax Act,1961.

(ix) Ensure compliance of service tax, trade tax and other duties and taxes.

Checklist- Quarterly

Revenue Checking

1.3 Verify and report non-recovery of:

(i) Locker rent

(ii) Folio charges

(iii) Penal interest for delayed/non-submission of returns, financial statement/stock statement required to be submitted

(iv) Penal interest on advances in respect of lapsed sanction/ limit

(v) Penal interest on excess over limit

(vi) Overdue interest on all types of bills, loans and packing credits for overdue period

(vii) Commitment fee for unutilized limit is collected as per rules

(viii) Commission of letter of credit, letter of guarantee and charges for safe custody, etc.

(x) Standing information charges

(xi) Stop payment charges

(xii) Processing fee on advances

(xiii) CIBIL charges, if applicable

(xiv) Lead bank charges

(xv) Cheque return charges

(xvi) Inspection charges

(xvii) Charges for documents under LC

(xviii) Charges for any services provided

(xix) Cheque-book issue charges

For rates, bank's service charges booklet/manual should be obtained and kept on record during the period of audit.

Checklist- Half yearly

1.4 Following is an illustrative half-yearly checklist:

(i) Physical verification of government and other securities held on behalf of Investment Department and timely collection of interest thereon and their maturity proceeds.

(ii) Compliance with insurance limit for cash and other fixed assets of branches.

(iii) Fixed and other assets at branch are serially numbered and recorded in fixed assets register, are adequately insured. Depreciation is calculated at head office or branch wise.

(iv) If office building is rented then check that rent agreement has been kept in safe custody, and the same has been renewed timely.

(v) Check whether customer service is satisfactory with regard to the following areas:

- Customer meeting has been convened as prescribed;
- Standing instructions are followed up;
- Complaint/suggestion box has been kept in branches;
- Staff dealing with customers at branch is polite to customers.

Chapter 2
Core Banking System

Background

2.1 Over the years, the banking operations have been atomized to a large extent and wide range of banking software's have been developed for accounting of transactions and core banking operations. Bank software's are becoming more sophisticated all the time. As new accounting methods develop and more people bank online, private banking software is being developed to streamline the processes.

Banking Industry and Banking Software

Current Scenario

2.2 The face of banking industry is changing continuously. What Banking is today is quite different from what it was in the years gone by. Some of the present trends in banking industry include following:

- Focus on Customer Relationship (Service Oriented Architecture[SOA]);
- Introduction of Value Added Services;
- Connectivity of branches;
- Multiplicity of Delivery Channels (ATM, Cash Deposit Machines, Cheque Deposit Machine, Point of Sale Units, Credit Card, Mobile Banking, Internet Banking);
- Focus on MIS and Risk Management;
- Focus on Reduction of Transaction Cost.

Future Scenario

2.3 One can visualize future scenario in the industry on current trends. Going by the current happenings one can expect the future of banking industry. Some of the important factors are as follows:

- Increase in the expectations of customers;
- Increase in healthy competition due to issue of new banking licenses;

- A greater variety of products and delivery channels in the market;
- Centralised customer management (Service centric approach);
- Information technology to act as an integrator and enabler between demands on the industry and services rendered.

Challenges

2.4 The biggest challenge before the banking industry today is posed by its customers' expectations. The customer today is more informed and aware than before. Customers demand more and more services and delivery channels. Customer's expectations are increasing with respect to anywhere, anytime banking and also for diverse products and facilities.

There are challenges posed by market forces due to stiff competition wherein the differentiator or selection of bank by the customers is based on quality of services. However, the service up-gradation comes with a cost for the bank. Hence, a trade-off between cost of transaction and quality service to customer is the key. Moreover, due to diversified products and services, upto date information for customer and banker is very important.

On the other front the regulatory requirements are rapidly increasing. Apart from handling transactions, customer and competition it is very important to pay equal attention to adherence to regulatory guidelines.

A composite system / software which handles transactions, customer relations, regulatory compliances, MIS/ reports request is the need of the hour. Core Banking Systems (CBS) provide the solution for the same. There are various Core Banking Software's available in the market. More prominent and used in India are Finacle, FLEXCUBE, TCS BaNCS.

Audit of Banks and Banking Softwares

2.5 Ever since the human being started documenting transactions, audit methodology and techniques have evolved over the period of time keeping pace with the style of business. With the growth in business volume and technological advances there has been paradigm shift in various aspects of business. Conducting audit of financial transactions cannot be an exception to the same. Traditional audit techniques and methodology were outcome of the volume and complexities of the business of its time. A classic example of the same is audit techniques applied for conducting audit of a bank operating under Core Banking System (CBS).

As we have witnessed, during the last decade there has been large scale growth in banking services, covering more and more geographical area and large number of population. This has necessitated applying modern technology, particularly in the field of data capturing, recording and processing. CBS is outcome of the same.

For obvious reasons audit methodology cannot remain static, it has also to change. Therefore, with the spread of CBS in large number of cases, changing audit methodology also became inevitable. If the auditor's dependence on technology hinges heavily, there is no reason why auditor should not apply the same technology.

Core Banking Solution (CBS)

What is CBS?

2.6 The core banking system is the set of basic software components that manage the services provided by a bank to its customers through its branches (branch network). The bank's customers can make their transactions from any branch, ATM, service outlets, internet, phone at their disposal.

The CBS is based on Service Oriented Architecture (SOA). It helps banks to reduce risk that can result from manual data entry and out of date information. It also helps banks to improve service delivery quality and time to its customer. The software is accessed from different branches of bank via communication lines like, telephones, satellite, internet, etc.

Core Banking System (CBS) works on a concept of Centralized Database and Processing. Transactions take place at various geographical locations which get recorded and processed at a Centralized Server. Updation of database is on Real Time Basis. Due to the centralization of transaction processing, issue of out of date information is eliminated. All the users connected to CBS will be able to get upto date information. CBS also enhances quality of reporting and strengthens access control.

Centralized Banking Solution/ Core Banking Solution

2.7 Under CBS data is stored in centralized servers at data centre. This effectively means that all operations at the connected branches, back offices are carried out through servers at data centre including transactions through other delivery channels like, ATMs, internet banking, phone banking, etc.

Under CBS, the branches, back offices are defined as SOL (i.e., Service Outlets) where each SOL functions as a service window. The CBS is capable of processing any transaction from any branch location connected to CBS. It can be equated with single window operations at airline counters or railway reservation counters wherein all the services can be obtained at one place. Hence, under CBS customer is now a customer of the bank and not merely a customer of a branch of the bank. This has facilitated anywhere, anytime banking convenience for the customer.

From bank's perspective, control over the application and processes has been entrusted at data center level. In addition to it, CBS also makes available effective MIS on real-time basis. It enables generation of all periodical returns centrally. As mentioned above, there are various CBS developed by various software companies available in the market and most commonly used are FINACLE, TCS BaNCS and Flex Cube.

Introduction to FINACLE

2.8 A Financial Package, for banking solution developed by Infosys on a platform of Oracle, is thus named as FINACLE. Presently, many Indian Public Sector Banks, Private Sector Banks and Foreign Banks operating in India are using this software as banking solution due to high flexibility and scalability. Finacle is an integrated, on-line, enterprise banking system designed to provide the "e-platform".

Prior to 1995 it was known as BANC 2000, a Total Branch Automation package with a distributed network. After 1995 Infosys developed the same as FINACLE, a Core Banking Solution. Functionalities of Finacle are as follows:

- Finacle facilitates anywhere banking.
- It is menu driven software with easy navigation.
- It is functionality rich and addresses the retail and corporate banking requirements.
- Customization and parameterization are two special features of Finacle.
- Finacle provides multi-lingual support.

- Finacle provides multi-level security, i.e., operation, database and application level security
- It supports workflow based transaction processing.
- It has high level of security control and audit capabilities.
- It has a common transaction interface for all type of transactions.
- It provides a browser based GUI interface to Finacle.
- SQL and PL SQL is used for generation of MIS, reports, queries at centralized level.
- Designed for optimum usage of network bandwidth.
- There are two functional modules:
  - *Retail and Corporate Module*- Encompassing Saving Accounts, Current Accounts, Term Deposits, Cash Credit Accounts, Overdraft Accounts, Term Loans, Demand Loans.
  - *Trade Finance Module* - Encompassing Inland & Foreign Bills, Forward Contracts, Inland & Foreign Documentary Credits, Inland & Foreign Bank Guarantees, Inland & Foreign Remittances and Pre-shipment Credits.

Security in Finacle

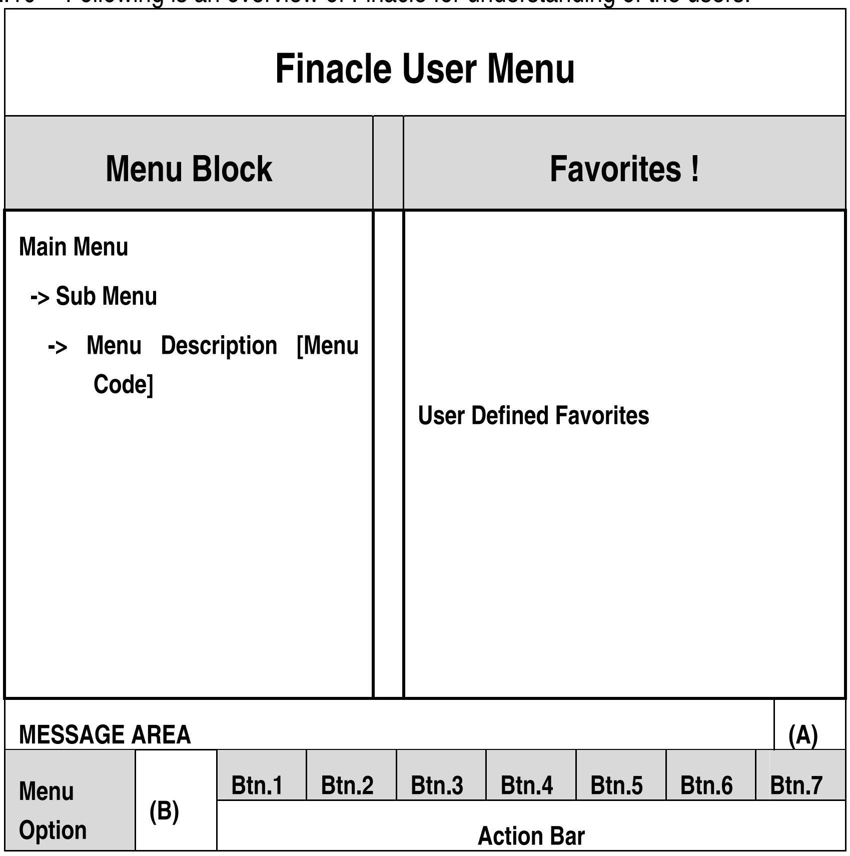
2.9 FINACLE is having multiple levels of security. Various security levels embedded in it are as follows:

- OS Level
  - No access to OS
  - OS and application level profile
  - Direct login to application menu
- Database level
  - Protection from external updating
- Application level
  - Menu level
  - User level

  - Product level
  - Account level
  - Transaction level
- Dual control for all transactions
  - Maker-Checker Concept
- Controlled error handling through exceptions
  - (1) Warning (2) Exception (3) Error

Finacle Overview

2.10 Following is an overview of Finacle for understanding of the users:



A = Progress Indicator

B = Field to Specify Menu Option

- *Menu Block*: The block houses all the menu and sub-menu options available in Finacle.
- *Menu Option Block*: Menu Code to be entered to gain access to the respective menu.
- *Action Bar* : User can execute the process of Finacle operations by clicking on various options on this bar. The hot keys are also assigned for all options, which appear on the bar.
- *Action Buttons*: Every action button has a specific purpose. For e.g., on clicking Who AmI button, system will display use rid of the user who is currently logged in and other information, viz., date and name of SOL in a message box.
- *Message Bar:* The message bar displays warnings, exceptions, errors or lists under a specific field code.
- *Favorites*: Menu items which are required and used on regular basis can be put in favorites by copying from Menu Block. As onetime process, specific menu item which is required to be copied to Favorites should be located in menu block and with the use of drag and drop the function can be stored under favorites menu.
- *Progress Indicator:* It shows the progress of the action initiated through the use of colours (i.e., **Green** indicates that the System is "Ready" for processing, **Red** indicates that the "System is busy in Processing Activity" and **Yellow** indicates that browser is performing internal processing like, assembling/ painting screen as per requirement. User should not operate the system)

General Key Map

2.11 Default Physical Keys in Finacle have been given in the table below. However, default key map differs in individual bank.

Physical Key	What does it do?
F1	Field level help. Like in several word processors and spreadsheet packages, F1 displays context sensitive help messages and field level help messages.
F2	List. This key lists the codes that may be used in a particular field.

Physical Key	What does it do?
F3 / ESC	Quit/ Back. Quits and takes the user back to where he started when in action. It can be used when the input is incorrect and the user wants to abandon what he has been doing. It can also be used to go back to the previous menu.
F4	Accept. After the user has completed the input, this key can be used to accept the data.
F5	Background Menu
F6	Next Block
F8	Copy Record
F9	Display Signature
F10	Commit/ Save. This is very important key and this concludes the transactions. This is the commit and transactions get into the General Ledger (database) when this key is used.
F11	Next field
F12	Previous Block
TAB	Go to next valid field
ENTER	Go to the next field
DOWN Arrow ↓ (Next Rec button)	Next Record (In a list or result of a query)
UP Arrow ↑ (PrecRec button)	Previous Record (In a list or result of a query)
CTRL+F1	Help maintenance
CTRL+F3	Show key map
CTRL+F4	Display error
CTRL+F8	Terminal lock

Physical Key	What does it do?
CTRL+F9	Memo pad look up
CTRL+F11	Context level help
CTRL+D	Page down on a list
CTRL+E	Explode. This key is particularly useful for the further inquiry.
CTRL+F	Clear field. This key combination can be used when the user wants to clear the field.
CTRL+T	Display LGI. The user ID, Terminal ID, SOL, BOD Date and language details are displayed.
CTRL+U	Page up on a list
CTRL+X	Put BOD date. This key combination populates the default BOD date in the field.
SHIFT+F4	Select the current item from the list. This key combination can be used to select a value from the list of valid values listed for a particular field.
SHIFT+F11	Transmit
SHIFT+TAB	Go to the previous field

Introduction to TCS BaNCS

2.12 A Financial Package, for Banking Solution offered by Tata Consulting Services. The Core Banking solution TCS BaNCS is an integrated solution that automates all aspects of core banking operations across entities, languages and currencies. BaNCS is built on open architecture, component-based product suite to leverage service-oriented and event-driven architectures. It's functionalities are as follows:

- Entire range of banking products including savings, checking, overdraft and deposit accounts.
- Entire range of lending products.
- Complement of transactional services including remittance, foreign exchange, cards and trade finance.

- Accessibility through multiple channels, including mobile banking and web.
- Full integration of front, middle, and back office processes.
- Accurate, timely and actionable information about customer relations.
- Single view between bank and customer.
- “Anytime anywhere” banking.

Introduction to Oracle Flex Cube

2.13 Flex Cube provides a comprehensive, integrated, interoperable, and modular solution that enables banks to manage evolving customer expectations. Major functionalities are as follows:

- 24/7 processing of large transaction volumes, with high availability.
- Multiple delivery channel support.
- Security management covering application and role-based access.
- Service-oriented architecture supports agile business process management.
- Componentized architecture helps build scalable and reusable solutions.

Quick Access Screens through Hot Keys in FlexCube

Hot Keys	Screen Name	Description
Alt + B	Balance Inquiry	This screen displays the account details of the savings and checking account balances such as the available balance, nucleated balance, current book balance, passbook balance, net balance, etc.
Alt + C	Customer Name And Address Inquiry	This screen displays the details such as, the name, address, city, country, SSN/TIN number, etc., of the selected customer.
Alt + A	Account Details	This screen displays the account details of the customer such as account number, account branch, account currency, customer name, etc.
Alt + S	Amount based Account Image Display	This screen displays the images on the basis of the details maintained in the Amount Based Operating Instruction Maintenance (Fast Path:

Hot Keys	Screen Name	Description
		7116) option.
Alt + P		This will enable the user to print the receipt of the transaction.
F8		This will enable the user to return to the same screen.

General Concepts of CBS and Finacle

SOL ID and Set ID (Init. Br. ID)

2.14 **SOL ID -**Under Core Banking System, each Branch, Back Office, Administrative/ Controlling Office are assigned a code, i.e., Service Outlet ID [SOL ID]. It helps in identifying the Branch / Office under which the Account is maintained. Hence, if a branch at Delhi is assigned a SOL ID of "0089", the accounts opened under Delhi Branch will display "0089" as SOL ID in CBS.

As discussed above under CBS any branch can initiate transaction for any of the account maintained with the bank. Hence, a distinction is required between the branch which maintains the account and the branch who initiate the transaction.

Set ID (Init. Br. ID): Set ID or Initiating Branch ID is a SOL ID of the Branch who initiated the transaction. For e.g., transaction of a cash withdrawal by a customer of Mumbai Branch (SOL ID "0044") from Delhi Branch (SOL ID "0089"). In the instant case "0089" is Init. Br. ID and "0044" is Account SOL ID.

In order to search transactions based on the branch who initiated transactions in Finacle, SET ID (Init. Br. ID) parameter is required to be used under Menu Code "FTI".

Tran ID, Journal No. and Date

2.15 Each transaction in Finacle will be assigned a unique Transaction ID. The Transaction ID remains unique only for the day, since, on the next day the Transaction IDs are reset.

Combination of Transaction ID and transaction date make it unique across the system. In Finacle, once the transaction is "Entered", a Tran ID is generated. To locate any transaction from the database the user need to use Tran ID and Date at TI/TM Menu command. Under BaNCS the transaction number is known as Journal Number.

(i) Transaction Type and Sub Type

Transactions in Finacle are entered with the Transaction Type and Transaction Sub Type. It is easier to trace set of transactions with Transaction Type and Sub Type.

Codes for Transaction Type and Sub Types are prescribed differently by each bank. For e.g.,

Transaction Type codes for Cash and Transfer may be of following types.

– Tran Type: Cash: “C”, Transfer: “T”

– Sub Tran Type: CR – Cash Receipt, CP: Cash Payment

The auditor must acquaint himself with the Transaction Types used by each bank. It helps auditors to design query (search parameters) for inquiry of financial transactions.

Customer Master Level Configurations

2.16 Under CBS, the customer is identified by a number, generally, called CUST ID/ CIF No. Following are the advantages of separate configuration for customer and accounts of customer:

(a) Identification of unique customers.

(b) Data redundancy can be reduced by eliminating the process of updating repetitive details about customer at each time of opening of account.

(c) It is easier to comply with customer centric regulations. For, e.g., TDS provisions under Income Tax Act (where payment to customer is important than payment for an account), IRAC Guidelines (where classification of account is borrower-wise and not account-wise).

(d) Multiple accounts of the customer can be mapped to a customer for better identification.

Under the Customer Master Level configuration basic details about the customer are updated. Details include name, date of birth, PAN number, etc.

2.17 Once the CUST ID/ CIF is opened, various accounts can be opened under the said CUST ID/ CIF. Relationship between CUST ID/CIF No. and account is that of parent and child wherein the Account Master inherits the information and parameter values from Customer Master.

In Finacle menu command **CUMM/ CUMI** is used for inquiry on CUST ID/ CIF No. Under BaNCS the customer master details can be reviewed through "Customer Master Details" module.

2.18. Some important points for auditors are as follows:

(i) Issues with multiple CUST-ID

In terms of guidelines issued by the RBI on UCIC, each customer in bank is required to be assigned a unique ID. However, it has been observed in many banks that multiple CUST IDs have been opened for a customer. It has also been observed that at the time of migration, it had migrated old customer information to one CUST ID and have opened new CUST IDs for opening of new accounts post migration.

Due to multiple CUST ID the very purpose of having configuration of CUST ID is defeated. The auditors should verify such discrepancies at the time of account opening verification. Moreover, the auditors should also seek help of bank's IT Dept. for generation of report based on combination of information, *viz.*, name, PAN, date of birth, employee code, etc., to identify existing cases of multiple CUST ID in the system.

At the time of opening of account, Finacle automatically displays the name of account holder based on CUST ID details. However, Finacle also allows user to amend the name. Generally, the said change is configured as an exception which requires sufficient powers/ work class in the system to override.

The auditor at the time of Account Opening verification should verify the details as per CUST ID and in account. Difference in names at both the places increases unwarranted confusion. Moreover, auditor should seek help of bank's IT Dept. for generation of report based on difference in name as per CUST ID and as per accounts opened (if any).

(ii) Account Level Configurations

Configurations/ parameters for are setup at the time of Account Opening. Modification afterwards is also permitted. Account Level master contains the parameters and details specifically with respect to account. For instance, Interest Rate, Interest payment periodicity, Freeze, Lien, etc.

It is important to note here that under CBS majority of functions and transactions are master driven and hence, any minor error at Master Level (whether Customer Master or Account Master) can have magnanimous effect on transaction processing. For e.g., if Interest Collection Flag is selected as "N" at Account Master Level, the system will not collect any interest. Hence, accuracy of master is a vital audit area.

(iii) Pointing Type Accounts/ Self Reconciling Accounts

Apart from maintaining customer accounts, the bank's general ledger also contains various Suspense/ Sundry Accounts. Such accounts can be with debit or credit balance. The said accounts are used for limited purpose and for parking of entries for limited time frame. Transactions wherein either debit/ credit leg is not confirmed/ identifiable at the time of transactions are parked in such accounts. For e.g., an amount of ₹ 1,000 is given to an employee in advance for purchase of stationery item for branch. The said transaction will be kept under such Suspense/ Sundry account till the date the employee submits the bill/ returns the advance.The transactions processed in such accounts are not routine hence it calls for continuous monitoring and earliest reversal. Moreover, numerous transactions in an office account make it difficult for reconciliation. In earlier times, the activity of reconciling the office account was manual.

However, under CBS such accounts are opened under Pointing Type Office Account/ Self Reconciling Accounts Scheme Code which facilitates automatic reconciliation and real-time information on outstanding/ non-reversed transactions. Transactions in such type of accounts are in two parts - Originating Transaction and Reversal Transaction. For each reversal entry, the system will prompt the user to point it to an originating transaction. There can be multiple reversals against single originating transaction. Such type of account will also ensure that in case of a debit type office account, credit entry as originating entry will not be permitted.

On the users side, at the time of reversal of Transaction the system will ask the user to "Point" the Originating Transaction against which the transaction is being reversed. On selection, the system will reduce the balance under the said Originating Transaction. Under this type of Pointing Type Account, at any given point of time aggregate of outstanding transaction-wise balance will be equal to the Office Account Ledger Balance. Under Finacle, verification of outstanding/ non-reversed entries can be verified from menu command **IOT (Inquire on Transaction)**. Moreover, a report on outstanding office account transaction can be generated through Menu **MSGOIRP**. Various customized reports for the said purpose are also available under each banks "Report" menu in Finacle.

Under BaNCS, the outstanding entries are available through offline reports viz. "Audit BGL accounts age wise break up"and "GL-Outstanding-Accounts" report.

(iv) Interest Table Maintenance

Interest collection as well as payment in CBS can be through Interest Tables or can be by way of absolute rate. In case a loan account wherein Interest Rate is based on a reference rate (say Base Rate), the Interest Rate field is updated with the Reference Rate Table to ensure automatic updation of Interest on subsequent change.

In case of Interest Table master, the primary rate is sourced from a Master Table. For instance, in case of Loan sanctioned as Base Rate + 3 % whereas Base Rate at the time of Sanction was 10%, the Interest Rate field will be updated either with BR+3 Table code or with BR Table with 3% updated in Account Preferential Debit Interest with +3%. Method of updation of interest may differ from bank to bank.

In case of few specialized products (e.g., subsidy linked accounts) limit level interest rate is required to be applied. In such case the parameters are setup at Interest Table Master Level and the said table code is updated under Interest Table field at Account Master Level.In case of a fixed rate loan, the interest rate is updated as absolute figure in Interest Rate field instead of Table. However, few banks follow the practice of updating "ZERO Interest Rate Table" with necessary interest rate at Account Preferential Debit Interest.

(a) Interest Flags

Values at Interest Flags determine the payment and collection of Interest. Applicable flags (i.e., Interest payment, Interest collection) are required to be updated at Account Master Level. Hence, if the Interest Collection Flag is updated as "N", there will not be charging of interest by system, although proper Interest Table Master is selected.

(b) Withholding Tax Flags

Interest payment to the customer is aggregated at Customer Master Level (i.e., for all the accounts opened under a CUST ID / CIF No.). The threshold limit for TDS is computed based on the amount aggregated at CUST ID Level. Once the payment of Interest exceeds minimum threshold level prescribed under Income Tax provisions, the system initiates deduction of taxes from Interest. However, for cases wherein customer has submitted Form 15H/ 15G/ tax exemption certificate, necessary flags are required to be updated to prevent deduction of taxes upto the enhanced limit (as applicable).

Withholding Tax flags are available at both CUST ID and Account Master Level. With the recent change in the Income Tax guidelines w.r.t. online submission of details of Form 15G/15H, the exemption is required to be flagged at CUST ID level for the amount of Interest Income declared by the customer.

In Finacle, withholding (TDS) flags are driven by Tax Slab. For each type of customer different tax slabs have been defined at Master Level e.g., TDS for individuals, TDS for corporate, TDS for exempt entities. It is important for auditor to verify correctness of Tax Slab vis a vis constitution of customer.

(c) Freeze Flags(Debit, Credit and Total)

In case of court order, dispute between the joint account holders, recovery notice from revenue authority the transactions in accounts are required to be suspended. Depending upon the requirement the transactions are suspended (viz. Debit, Credit or all) through Freeze Flags.

The freeze can be applied at CUST ID Level (i.e., all the accounts of the customer) or specific account of the customer. The source documents are required to be verified for marking of freeze and unfreeze event. The inquiry of accounts with Freeze Flag can be made in Finacle through ACS Menu Command with Freeze Flag as "T"=Total Freeze, "D"=Debit Freeze, "C"=Credit Freeze.

(d) Schemes and Scheme Codes

Different types of account products are offered to customer with different characteristics. For instance, various types of Savings Accounts are offered. The aggregation of account balance for such cases will take place at Sub GL & GL Level. However, for account operations and account master setup different schemes are setup in CBS. Scheme Code acts as a placeholder. Inquiry for different types of accounts can be made in Finacle through ACS Menu Command with "Scheme Code".

Exception Types

2.19 The transaction errors are handled in CBS through following modes:

- Warning – Warns user for possible errors based on prefixed criteria
- Exception – Allows user (with sufficient power) to override. However, the transaction will be recorded in Exception Report for the day
- Error – Does not allow user to proceed further, unless the correct values are filled in.

Maker and Checker Matrix for Valid Transaction

2.20 Under CBS the transactions are processed by atleast two officials of the bank under Maker and Checker mode. The same is tracked through the transaction events (viz. entry, posting and verification). Posting is the event which updates the GL Balance. Posting activity depends on the rights assigned to each user ID.

Inventory Locations

2.21 The inventory concept under CBS refers to handling of security stationeries, viz., Non-personalized cheque books, Demand Drafts, Term Deposit Receipts. Each bank, as per the requirement, creates different inventory location and inventory sub location codes in CBS.

Predominantly, locations are created for joint custody (dual custody), employee custody, external locations. Barring, external location, balancing of security stationery is available for all the locations.

In Finacle the report on outstanding inventory items can be generated through Menu command ISRA. Whereas under BaNCS the same set of reports can be generated through VPIS (Valuable Paper Inventory System) module.

Zones in Clearing Modules

2.22 For easy identification of type of cheque and proper reconciliation various zones are opened on daily basis (as per clearing cycle) in CBS. Various zones are opened for Non CTS Cheques, Inter-bank Cheque, KYC Cheques, MICR Cheques, Non-MICR Cheques, Warrants, CMS Cheques, etc. Opening of Zone is the primary event before lodging any Inward Clearing instrument or Outward Clearing Instrument.

Limit and Limit Node

2.23 Under Finacle the Limit Management is done through Limit Node Maintenance. Wherein, the limits are specified at each node level with capping. Credit Limits can be set at Account Level as well as at Node Level for deriving the Drawing Power for a customer. Setting up of Limit at Node level has following advantages:

- Managing two or more accounts with drawing power deriving from the same security.
- Interchangeability of limits among different accounts.
- Monitoring the overall exposure to a single client/ group of clients.
- Exposure to a select commodity/ security. *Limit Node Maintenance* helps to build these requirements in the limit management

Limit Node

2.24 Limit nodes are used to group accounts under one node to enable easy monitoring and organization. A limit node can be linked to a security for deriving drawing power. Distribution of overall group (group may be a group of clients or a group of accounts) limits to individual members (members may be accounts or clients) is possible through creation of Parent Node and Child Nodes. Every child node can further be distributed to group of accounts or clients. This is diagrammatically explained through below example.

Facility Type	Particulars	Limit (Rs. Lacs)	Remarks
Funded	Term Loan	225	
	WCDL	75	Funded Limit Cap is 500 Lacs *Upper Limits fixed in each type of Facility*
	CC	200	
	BP / FBP / BD	50	
Total Funded Facilities		**500**	
Non-Funded	LC	300	Non Funded capping is at Rs. 500 Lacs
	BG	300	
Total Non-Funded Facilities		**500**	
Total Company Exposure		**1000**	**Total Exposure to Company should not exceed 1,000 Lacs**

Temporary Overdraft (TOD) Setup

2.25 Granting of TOD to a customer is a credit decision from bank's perspective. Concurrent auditor has to review the source documents and delegated powers to ascertain whether the sanction was inline with the guidelines prescribed by the bank. Setup of TOD is done in Finacle as follows. TOD is granted to an account under various circumstances. For instance:

Type	Event	Mode
TODIC	Interest Calculation	Single
TODDL	Drop in Limit	Single
TODMN / TODUG	Manual / User Generated	Single/ Running/ Adhoc

Explanation of various TOD modes is as follows.

Mode	Narrative
Single (S)	It refers to TOD for specific purpose/ transaction. It can be used only for the specific transaction during which the same was granted.
Running (R)	It refers to setting up of a parallel limit at account level for a defined period over and above credit limits (if any).
Adhoc (A)	Adhoc allows customer with OD / CC Accounts to operate within TOD Limits for defined period.

2.26 From above narrative it appears that running and adhoc TODs serve the same purpose. However, from CBS perspective, both the events are different. In case of single and running TOD, CBS computes the number of TOD sanctioned in the account. In case the cumulative number exceeds the prescribed limit for an account, an exception gets triggered for all subsequent transactions. Whereas in case of adhoc TOD the said TOD is not counted under number of TODs thereby circumventing the exception controls embedded in the system.

It is important for auditors to verify cases wherein adhoc Limits have not been delinked on expiry in system.

Register Type and Subtype (Trade Transactions)

2.27 The concept of Register Type and Sub Type is same as Transaction Type and sub types as discussed above. The types are used to aggregate transactions of same nature in system. It helps in identifying and tracking of transaction in a better manner. In Finacle, Register Type and Sub Types have been used in Inland Trade Transaction and Foreign Trade Transactions modules.

List of few Register Types and Subtypes for an Import Transactions is as follows:

Reg. Type	Sub Type
Import Bill on Collection	Sight
Import Bill on Collection	Usance
Import Bill under LC	Sight
Import Bill under LC	Usance

Direct Import Bill	TT (Telegraphic Transfer) / DD (Foreign Demand Draft)
Advance Remittance against Import	TT (Telegraphic Transfer) / DD (Foreign Demand Draft)

Auditing through CBS

2.28 Generally, the following set of steps is recommended at the start of the audit to understand the operations at the branch level and familiarize oneself with the branch and its team:

- Document list of software's, applications and interface details associated with CBS.
- Review Usage Manual or Document Software navigation options and Menu Codes.
- Document list of Reports available in CBS and its menu codes.
- Review Exception Reports/ MIS Reports generated by Data Center.
- Review access rights, limited access and free access.

Parameters Affecting Automatic Identification of NPAs and Re-designing of Audit Processes

2.29 In terms of directives issued by Ministry of Finance and Reserve Bank of India, it is mandatory for banks to identify the bad loans through CBS/ Systems instead of conventional methods. CBS like other software work on GIGO principle. Master Data play an important role in correct identification of Bad Loans.

Following are few scenarios wherein incorrect updation in Master Data, manipulation through transactions etc. may impact correct identification of bad loans through CBS.

Parameters	Auditors' Primary Checks	Suggested System Support
Discrepancies in setting up the EMI / Instalments	➢ Whether EMI/ instalment is correctly setup. ➢ Whether EMI/	**<u>Finacle:</u>** – ACI -> Option "E" Repayment details **<u>BaNCS:</u>**

Parameters	Auditors' Primary Checks	Suggested System Support
	instalment amount is matching with the Sanctioned Terms. ➢ Whether periodicity of Instalment is correctly classified as per Sanctioned Terms?	– DL/TL Accounts & Services ➔ Enquiries ➔ Account – Deposit / CC / OD Accounts & Services ➔ Enquiries ➔ Deposit / CC / OD Account ***(Short & Long Inquiry options are available under both menu.)***
Multiple sets of EMI / Instalments	➢ For case of Multiple sets of EMI e.g. For 1-5 years EMI of ₹ 7,000 and after 5 years ₹ 7,500 ➢ Whether sets of EMI are properly entered? ➢ Is there any substantial difference between 1st set of EMI and 2nd or other sets (e.g. 1st set ₹ 5,000 and 2nd ₹1,00,000) which cast doubt on debt serviceability?	**<u>Finacle:</u>** – ACI -> Option "E" Repayment details **<u>BaNCS:</u>** – DL/TL Accounts & Services ➔ Enquiries ➔ Account – Deposit / CC / OD Accounts & Services ➔ Enquiries ➔ Deposit / CC / OD Account ***(Short & Long Inquiry options are available under both menu.)***

Parameters	Auditors' Primary Checks	Suggested System Support
System determined Asset Classification vis a vis User defined Asset Classification	➢ CBS contains two sets of parameters. At first instance CBS identify the account based on set parameters under Asset Classification types. ➢ In few CBS it has been observed that user is generally given the option to differ and select/ amend the classification. In such cases detailed scrutiny of NPA system is required to be carried out. ➢ Due to errors in certain Master Data, there can be erroneous identification of account as NPA. However, such accounts require detailed scrutiny.	**<u>Finacle:</u>** ➢ ACM/ ACI Option – 'Y' Asset Classification Inquiry ➢ A report containing accounts wherein there is difference between Asset Classification by System and by user should be requested for. Accounts listed in the said report should be thoroughly verified.

Parameters	Auditors' Primary Checks	Suggested System Support
Manipulation in SL / DP	➢ Changes in SL / DP should be cross checked with Sanctioned Letter. ➢ Whether any change in Limit is supported by necessary documentation?	**Finacle:** ➢ ACLHM – Account Limit History Maintenance **BaNCS:** ➢ Tailor-made report on Changes in Account Limits
Incorrect moratorium period	➢ Based on moratorium period CBS will identify the Loan Instalment and will track repayment. ➢ In case the moratorium period / instalment start date is erroneously updated system will not show correct result.	**Finacle:** ➢ ACI – Option "E" – Repayment Details **BaNCS:** ➢ Account Master details (Long Inquiry)
Re-phasement without reporting it as reschedule	➢ Loan Account Instalments are rephased / recalibrated without reporting the same as Re-schedule. ➢ Verify whether any change in Repayment instruction is made through System. Compare the said accounts with list of Restructured	**Finacle:** ➢ ACI – Option "E" – Repayment Details **BaNCS:** ➢ Account Master details (Long Inquiry) ➢ Report containing details of all the cases wherein EMI / Instalment is changed should be sought

Parameters	Auditors' Primary Checks	Suggested System Support
	Accounts.	
Instalment Start Date is Future Date	➢ Check whether Instalment Start Date entered as per sanctioned term? ➢ In case of future date system will not identify instalment and any repayment received will be shown as "Overflow".	**Finacle:** ➢ ACI – Option "E" – Repayment Details **BaNCS:** ➢ Account Master details (Long Inquiry)
Interest Demand date (Future Date)	➢ Check whether Interest Start Date entered is as per Sanctioned Term? ➢ In case of future date as Interest Demand Date system will not accrue interest and any repayment received will be shown as "Overflow".	**Finacle:** ➢ ACI – Option "E" – Repayment Details **BaNCS:** ➢ Account Master details (Long Inquiry)
Fictitious credit through Office Account / Inter-branch Account	➢ Are there any quarter/ year end credits cited in the account? ➢ Check the source of Credit Entries. ➢ Review transactions in Office Accounts/ Inter Branch Accounts.	**Finacle:** ➢ ACLI – (Use CTRL + E to Explore the Tran) ➢ Review of Office Account Ledgers **BaNCS:** ➢ Deposit / CC / OD Accounts & Services ➔ Enquiries ➔ Transaction

Parameters	Auditors' Primary Checks	Suggested System Support
		➢ DL/TL Accounts & Services ➔ Enquiries ➔ Transaction
Round tripping from internal accounts	➢ Close scrutiny of transaction and review of chain/ series of transaction for accounts with deficiency is required. ➢ Such transactions will inflate the Credit Turnover in the account.	**Finacle:** ➢ ACLI – (Use CTRL + E to Explore the Tran) ➢ Using only Account Turnover Information generated through "ATOR" / "CUTI" / "ACTI" menu may lead to incorrect inference, since the credits are not solitary credits in account. **BaNCS:** ➢ Deposit / CC / OD Accounts & Services ➔ Enquiries ➔ Transaction ➢ DL/TL Accounts & Services ➔ Enquiries ➔ Transaction
Temporary Overdrafts	➢ Check whether the TOD is sanctioned in order to bring the overdrawn limit to base level additional facility through TOD is sanctioned.	**Finacle:** ➢ ACLI – Option "O" ➢ TODRP – TOD Register Printing **BaNCS:** TOD Report

Parameters	Auditors' Primary Checks	Suggested System Support
Devolved bills parked in Office Accounts and not in limit account	➢ Devolved Bills under LCs are required to be debited to the Limit Accounts only. Assessment of Asset Classification will be based on composite overdrawn portion Limit + LC Devolved amount (if any on devolvement) ➢ Check whether the amount of devolvement of LC backed bills are parked in Office Accounts or any separate account?	**Finacle:** ➢ BI & FBI – with Bill Status as "K" using status date filter **BaNCS:** Report on Devolved bills under Import LC
Multiple CUST ID to prevent the other account from becoming NPA	➢ Check whether multiple CUST IDs have been opened for the borrower with different accounts? ➢ NPA Report and search all the case by few characters ofName.	**Finacle:** ➢ ACS – Account Selection (Search based on Name) ➢ LAGI – Loan Account General Inquiry (Inquiry based on other parameters) **BaNCS:** ➢ Customer Management ➔ Enquiries ➔ Search by Name

Parameters Affecting Collection of Interest/ Revenue

2.30 Primary revenue for banks is interest on loans and advances. Charging of interest is completely automated barring few products. However, the processing is based on certain important parameters. System parameters / fields which affect the interest computation should be thoroughly verified. Some important interest parameters are as follows:

(i) Interest Table
- ➢ Debit Interest Rate and Credit Interest Rate
  - – Interest Version
  - – Currency
  - – Limit Level Interest
- ➢ Penal Interest

(ii) Interest Rate (Static/Absolute and Based on Ref. Rate)

(iii) Interest Preferential Customer Level **-** Interest rate preference will be applied to all the accounts of the customer based on type of Interest.
- ➢ Debit Interest Preferential
  - – Positive preference value
  - – Negative preference value
- ➢ Credit Interest Preferential
  - – Positive preference value
  - – Negative preference value

(iv) Interest Preferential Account Level **-** Interest rate preference will be applied to the specific account wherein the preference is updated.
- ➢ Debit Interest Preferential
  - – Positive preference value
  - – Negative preference value
- ➢ Credit Interest Preferential
  - – Positive preference value
  - – Negative preference value

(v) System Support / Important Menu Codes:
- ➢ <u>Finacle:</u> INTCI, AINTRPT, INTPRF, INTTM
- ➢ <u>TCS Bancs:</u> i) OD/CC Accounts -> Interest Rate History ii) DL / TL -> Interest Rate History

2.31 Following are few events/ scenarios wherein there is a possibility of non-application/ incorrect application of Interest:

Sr. No.	Event / Scenario
1	Interest pegging in Advance Accounts set as "Y". (If "Y" is selected, system will charge interest at the rate prevailing at the time of Account Opening. For the cases of Fixed Rate Loans Pegging Flag will be "Y")
2	Future Date is updated in Interest Demand Date
3	Interest on Principal / Payment of Interest Flag is set as "N"
4	Effective Rate of Interest is updated as "0"
5	Account Open and Instalment Start Dates are identical
6	Account Open and Interest Demand Dates are identical
7	Interest Table Code "Zero" is selected
8	Interest Demand Date is Past Date
9	Interest Demand Frequency is Blank

Audit of Foreign Exchange Transactions with the Use of CBS

2.32 The liberalization of economy is paving way for opening of new areas for inbound and outbound investment. Moreover, with the increase in the global trade the foreign exchange and cross border transactions are increasing at a rapid speed. However, it also poses challenge of preventing misuse of regulations and money laundering activities.

2.33 Following are few activities that the auditor must carry out for concurrent audit of Foreign Exchange Transactions:

Audit Activity	Important Menu Codes of Finacle
Review of Letter of Credits issued, Expired, Search on Outstanding LCs	For Inquiry – DCQRY For Report – DCREG, DCRPTS, DCSTMT
Review of Bank Guarantee issued, invoked, closed, outstanding, Search on expired BGs	For Inquiry – GI For Report – GILR, GPI

Audit Activity	Important Menu Codes of Finacle
Audit of Inland Bills (under collection, under LC, discounted)	For search: BI Search result printing: BP For specific bill: BM
Audit of outstanding Inland Bills	Report – BRCR (Collection Bills), BRBPR (Purchased Bills)
Audit of Foreign Bills (under collection, under LC, discounted)	For search: FBI Search result printing: FBP For specific bill: FBM
Audit of outstanding Foreign Bills	Report – FBBR
Audit of Inward and Outward Remittances (Other than Import and Export Transactions)	For Inward Remittance: IRM For Outward Remittance: ORM
Tracking of Packing Credit granted and tracking of order in case of Running Packing Credit	Account wise Packing Credit: ACLI Running Packing Credit: RPCTM

Audit of Office Account Transactions through CBS

2.34 Office accounts are opened for the purpose of parking entries till the time the final effect is not determined. However, at various occasions it has been observed that the entries remain in the said parking accounts for a long period. Moreover, in case of weak monitoring of the said accounts, the Office Accounts are susceptible to fraud and misappropriation. There are various types of office accounts:

(i) Based on Functionality

- Pointing Type/ Self Reconciling Accounts
- Non Pointing Type Accounts

(ii) Based on Type of Entry

- Sundry Accounts, Suspense Accounts
- EOD/BOD Check Accounts

- Inter branch Account
- Mirror Accounts
- Pool Accounts

2.35 Following are few audit actionables for concurrent auditor carrying out audit of Office Account Transactions:

Events	Audit actionable	Suggested system support
Cash Payment from Office Accounts	Authorization of Transaction as per Delegated Authority	**Finacle:** • ACLI – For Transaction • FTI – For Search **BaNCS:** • BGL -> Enquire -> Transaction
TOD through Office Accounts	Through ineligible credit originating from a office account, customer can be accommodated. It also circumvent the number of TODs granted to customer. Moreover, interest will not be applied in the said case.	**Finacle:** • ACLI – For Transaction in Office Account **BaNCS:** • BGL -> Enquire -> Transaction
Parking of Cash Difference in Office Accounts, Clearing/ Remittance differences through Office Accounts	Difference in Reconciliation, Cash Shortage debited to Office Account and not reversed. Review ledger account in detailed on monthly basis.	**Finacle:** • ACLI – For Transaction in Office Account • IOT – For inquiry on outstanding transaction • MSGOIRP – For

Events	Audit actionable	Suggested system support
		Printing of outstanding office account transaction report **<u>BaNCS:</u>** • BGL -> Enquire -> Transaction • “Outstanding BGL Transaction” Report
Rotation of entries in Office Accounts	To prevent entry being reported as long outstanding entry, a new transaction with debit and credit leg in the same account is posted. Thus, the system considers the new transaction date for reporting as outstanding entries. Review transactions with same Debit and Credit amount through Ledger Scrutiny	**<u>Finacle:</u>** • ACLI – For Transaction in Office Account **<u>BaNCS:</u>** • BGL -> Enquire -> Transaction
Correctness in mapping of reversal transaction to originating transaction	If the transactions have not been reversed against the related originating entries the report generated by CBS will show incorrect outstanding items.	**<u>Finacle:</u>** • ACLI – For Reversal Transaction in Office Account **<u>BaNCS:</u>** • BGL -> Enquire -> Transaction

Events	Audit actionable	Suggested system support
Value Dated (Back Dated) Transactions	Transaction credited in the advance type accounts, Operative accounts with a value date (Back date) wherein the clear funds were not available in the office accounts. Review the transactions from Revenue Leakage perspective.	**<u>Finacle:</u>** • ACLI – For Transaction in Office Account • FTI – For Value Dated Transaction **<u>BaNCS:</u>** • BGL -> Enquire -> Transaction
Round Tripping	Rotation of entry from office account to operative account(s) without any justification/ source document. Review the transactions from the perspective of inflating credit turnover of account.	**<u>Finacle:</u>** • ACLI – For Transaction in Office Account **<u>BaNCS:</u>** • BGL -> Enquire -> Transaction
Advance paid for Fixed Assets not capitalized	Entries for payment of advance against procurement of Fixed Assets not reversed.	**<u>Finacle:</u>** • ACLI – For Transaction in Office Account • IOT – For inquiry on outstanding transaction • MSGOIRP – For Printing of outstanding office account transaction report

Events	Audit actionable	Suggested system support
		BaNCS: • BGL -> Enquire -> Transaction • "Outstanding BGL Transaction" Report
Income realized not credited to Revenue Account	Loan Instalment received from Customer, not adjusted. Processing Fees received, not credited to Income Account Charges collected, not credit to Income Account	**Finacle:** • ACLI – For Transaction in Office Account • IOT – For inquiry on outstanding transaction • MSGOIRP – For Printing of outstanding office account transaction report **BaNCS:** • BGL -> Enquire -> Transaction • "Outstanding BGL Transaction" Report

Manual Updation in CBS and its Verification Aspects

2.36 Under any CBS the transactions are processed as per pre-defined process. Majority of the processes in CBS are automated and based on masters. A manual intervention in automated process leads to error in transaction processing.

Following are few manual changes/ modification in system which affects the transaction processing. The concurrent auditor must review the manual updation in CBS on monthly basis:

Manual Entry	Probable impact
Advances	
Interest Rate change	Revenue Leakage, Excess collection of Interest
Change in EMI	Revenue Leakage, NPA Identification
Processing of transactions against un-cleared outward clearing effect	Recovery of amount from customer in case of cheque return
Backdated Renewal Date updation (Updating Date of Renewal on running date with past date)	NPA Identification
Change in Limit – From Non Fund Base to Fund Base	NPA Identification
Account & Customer Master	
Tax exemption updation	Non compliance with TDS provisions
Dormant to Active	Susceptible to fraud
Interest Table Code as "0"	Revenue Leakage
Interest Collection Flag "N"	Revenue Leakage
Reclassification of Agriculture Advance as per revised RBI norms dt. April 23, 2015	Sectorial Classification
Foreign Exchange Transactions	
Erroneous Foreign Exchange Rate	Revenue Leakage, Accommodation to customer
Full BOE received flag marked as "Y" wherein BOE for entire transaction is not received	Reporting to RBI under BEF Return
FIRC Issuance (without updating flag printed "Y")	Duplicate issuance of FIRC without "Duplicate FIRC" inscription.

Manual Entry	Probable impact
Merchant Trade Transaction (Manual mapping)	Reporting to RBI
Transaction Processing & Housekeeping	
Changes / Modification in Auto Calculated charge amount at the time of posting of transaction	Revenue Leakage
Ineligible Credits to NRE and FCRA Accounts	Non-compliance of FEMA Guidelines
ATM Replenishment entries	Susceptible to Fraud
Payment for FD Closure proceeds in Cash through Office Accounts in excess of ₹ 20,000	Non-compliance with Income Tax Guidelines
Revalidation of Old DDs	Susceptible to Fraud
Value Dating (Credit Transactions in CC / OD Account with Value Date without Value Dating at Debit Leg)	Revenue Leakage
Debit to Income Account (though Transaction Maintenance Menu)	Revenue Leakage
Manual Credit to Income Account (though Transaction Maintenance Menu)	Revenue Leakage (Computation of Income credited to be verified)
RTGS / NEFT in cash through office accounts > 49,999	Non-compliance with AML guidelines
Delay in posting of clearing cheque return	Accommodation to customer
Manual Transfer of Security Stationery from Inventory location to External Location	Susceptible to Fraud (Avoid reporting of missing inventory)

Generation and Verification of Specific Reports Based on Various Criteria

2.37 CBS allows generation of various reports through frontend as well as through backend. Few important reports for review by concurrent auditors are as follows:

(a) Exception Report

Reports for the month end and two days prior and after month end should be verified. Exceptions of following natures should be closely verified:

(i) Balance exceeded Account Limit

(ii) Manual debits to Income Account

(iii) Value Dated Transactions

(iv) Manual entry for SI Failure cases

(v) Instrument passed against Clearing

(vi) Backdated entries (normally restricted)

(b) Irregularity Report

Reports for the month end and two days prior and after month end should be verified. Report contains details of Accounts where Balance in Accounts are greater than the limits sanctioned. Check whether the same is due to:

(i) Application of Interest

(ii) Granting of Intra Day TOD

(iii) Passing of Instruments against Clearing Effects

(c) Accounts where Interest Code is '0'

Interest will not be charged from Accounts where Interest Code is selected as '0'. Hence, a detailed checking is required. Possible reasons can be if it is a NPA account or an account with a moratorium.

(d) Interest Collection Flag as "No"

If Interest Collection Flag is selected as "No", Software will not consider the account for calculation and entry for Debit Interest.

(e) Debit Interest SI Failed Report

Failure of Standing Instruction for Debit Interest should be closely verified. If the SI is failed the Account will not be debited for Interest. SI Failure can be for any reason like:

(i) Non-availability of Balance in Account (In case of TOD in Operative Account)

(ii) Non-availability of Limit in Account

(iii) Technical Snag in execution

Whether Branch has manually passed the entry for all such cases should be verified.

(f) Loan Instalment SI Failed Report

Same as above.

(g) Report containing all Advance Accounts with Limits

Generally, CBS Softwares generate a Report wherein details of all Advance Accounts are listed. Excel can be used to verify cases of DP > SL, Margin Requirement, etc.

(h) TOD Report

Documents and sanction orders should be verified for all the cases of Manually granted TODs. In Finacle the report can be generated through Menu Code "TODRP".

(i) Account Turnover Report

To review the quantum of transactions in the borrower accounts turnover reports should be used. In Finacle, inquiry for Account Turnover can be carried out through "ACTI, CUTI" Menu codes and report can be generated through "ATOR" Menu.

(j) Loan Inquiry

In Finacle, criterion based search for Loan Accounts is available through Menu option "LAGI". The said menu can be used to verify:

- New sanction, Accounts closed
- Loans under various schemes
- Loans based on Account Classifications
- Accounts search based on Limit (Credit & Stock Audit)

(k) Loan Overdue Inquiry

In Finacle, criterion based search for Overdue & Overflow Loan Accounts is available through Menu option "LAOPI". In case of BaNCS the said details are available through offline daily report. The said menu can be used to verify:

- Principle & Interest Overdue and Overflow
- Overdue in "%" as well as Overdue in "No. of Days"

(l) Financial Transaction Inquiry

In Finacle, report based on different criteria for financial transactions can be generated through Menu Option "FTR". The said menu can be used to verify:

- Loan disbursement in Cash (Sub GL code & Tran Type)
- Value Dated Transactions verification (Only value dated flag)
- Transactions in Loan / OD-CC Accounts (SubGL, Tran Type, Part Tran Type)
- Credits to NRE Accounts in a period (Sub GL, Part Tran Type)
- Credits to FCRA Accounts in a period (Sub GL, Part Tran Type)
- Cash Deposit Transactions above Rs. 50,000 to verify compliance with Income Tax Guidelines on PAN (Tran Type, Tran Sub Type)
- Cash Transactions above Rs. 10 Lacs to verify compliance with AML Guidelines (Tran Type)
- Debits to ESCROW Accounts to verify compliance with ESCROW Agreement (Sub GL, Part Tran Type)

Guide on Audit Activity through CBS for LFAR and Tax Audit Requirements

2.38 Each bank uses its own format for concurrent audits. A common report format used by all the banks is of Long Form Audit Report (issued by statutory auditor). Following are few checkpoints for concurrent auditors alongwith suggested system support.

Audit Activity / Process / Audit Area	**Auditors' Primary Checks**	**Suggested System Support**
Cash	➢ Physical verification of Cash Balance ➢ Cash Balance as on the date of Audit Period ➢ Cash Balances reported in Friday Statement	**Finacle:** ➢ "**ACLI**" - Account Ledger Inquiry (Vault A/c and Teller Accounts) **BaNCS:** ➢ → Reports → Cash Related → View Cash Summary (Click on Fetch) ➢ → Branch Reports → Cash Officer's Jotting Book Report ➢ → Reports → Printing Reports → Cashier / Teller Cash Report
Balances with RBI / SBI / Other Banks	➢ Balance as on Date ➢ Transactions in Mirror Accounts ➢ Reconciliation Statement (Generally outside of CBS)	**Finacle:** ➢ "ACLI" - Account Ledger Inquiry **BaNCS:** ➢ → Branch Accounting (BGL) → Enquire → Transaction
Advances	➢ Sanction Limit / Drawing Power setup	**Finacle:** ➢ "**ACLHM**" – Account Limit History Maintenance ➢ "**ACM / ACI**" – Account Master (Go to Limit details) ➢ "**LTL**" – Limit Tree Lookup (Tree view of all Limits)

Audit Activity / Process / Audit Area	Auditors' Primary Checks	Suggested System Support
		BaNCS: ➢ DL/TL Accounts & Services ➔ Enquiries ➔ Account ➢ Deposit / CC / OD Accounts & Services ➔ Enquiries ➔ Deposit / CC / OD Account
Advances	➢ Account & Customer Master parameters setup viz., ➢ Interest Parameters (Regular & Penal Interest) ➢ Repayment Instructions ➢ Standing Instructions (SI) Parameters	**Finacle:** ➢ "**ACLHM**" – Account Limit History Maintenance for DP & SL – Account Specific ➢ "**ACM / ACI**" – Account Master ➢ "**CUMM / CUMI** " – Customer Master **BaNCS:** ➢ DL/TL Accounts & Services ➔ Enquiries ➔ Account ➢ Deposit / CC / OD Accounts & Services ➔ Enquiries ➔ Deposit / CC / OD Account ***(Short & Long Inquiry options are available under both menu.)***
Advances	➢ Transactions in Borrower's Account	**Finacle:** ➢ "**ACLI**" - Account Ledger Inquiry **BaNCS:** ➢ Deposit / CC / OD Accounts & Services ➔ Enquiries ➔ Transaction ➢ DL/TL Accounts & Services ➔ Enquiries ➔ Transaction

Audit Activity / Process / Audit Area	Auditors' Primary Checks	Suggested System Support
Advances	➢ Interest Rate History	**Finacle:** ➢ "**INTTM**" – Interest Table Master Maintenance (Under Inquire Mode – Account Specific) **BaNCS:** ➢ Deposit / CC / OD Accounts & Services ➔ Interest Rate History ➢ DL/TL Accounts & Services ➔ Interest Rate History
Advances	➢ Conduct of Account and Credit Turnover ➢ Turnover of CC Account based on Borrower's Business profile ➢ In case of Loan accounts **ACTUAL** recovery of Installments and Interest	**Finacle:** ➢ "**ATOR**" – Account Turnover Report ➢ "**ACTI**" – Account Turnover Inquiry ➢ "**CUTI**" – Customer Level Turnover Inquiry **BaNCS:** ➢ DL / TL Accounts & Services ➔Enquiries ➔Long ➢ Deposit/CC/OD Accounts & Services ➔Enquiries ➔Long
Advances	➢ Non Performing Asset ➢ Search an Account based on Criteria	**Finacle:** ➢ "**ACS**" – Account Selection (2nd Screen – IRAC Code – Main Asset Classification)

Audit Activity / Process / Audit Area	Auditors' Primary Checks	Suggested System Support
		BaNCS: ➢ DL / TL Accounts & Services ➔Enquiries ➔Short ➔ Select Option "1" – TL / DL ***[Long Inquiry for NPA Date]*** ➢ Deposit/CC/OD Accounts & Services ➔Enquiries ➔Short ➔ Select Option "2" – CC / OD ***[Long Inquiry for NPA Date]*** ➢ Common Processing ➔Overdue / NPA ➔NPA Enquiry (Risk Grade Inquiry / NPA Status Inquiry)
Advances	➢ Interest Report	**Finacle:** ➢ "**AINTRPT**" – Interest Report for Account **BaNCS:** ➢ Product Sheets – To be requested from Data Center (if not available through user login)
Advances	➢ Primary & Collateral Security Maintenance	**Finacle:** ➢ "**SRM**" – Security Register Maintenance **BaNCS:** ➢ DL/ TL Accounts & Services ➔ Security (Primary/ Collateral) ➔Customer ➔ Amend / Enquiry ➔Amend / Enquire Security

Audit Activity / Process / Audit Area	**Auditors' Primary Checks**	**Suggested System Support**
Advances	➢ Lien Marking	**<u>Finacle:</u>** ➢ "**ALM**" – Account Lien Maintenance **<u>BaNCS:</u>** ➢ DL/ TL Accounts & Services ➔ Security (Primary/ Collateral) ➔Customer ➔ Amend / Enquiry ➔Amend / Enquire Security ***(Under BaNCS – Collateral ID is required to be created before setting up limits)***
Advances	➢ Account Ledger Printing	**<u>Finacle:</u>** ➢ "**PSP**" – Pass Sheet Print ➢ "**ACLPCA**" – Customer Ledger Account Print **<u>BaNCS:</u>** ➢ **Print Menu** available under DL / TL Accounts & Services and Deposit / CC / OD Accounts & Services
Advances	➢ Non Fund based Facility (LC, BG)	**<u>Finacle:</u>** ➢ "**GI**" – Guarantee Inquiry ➢ "**DCQRY**" – Documentary Credit Query **<u>BaNCS:</u>** ➢ Report generated from Trade module

Audit Activity / Process / Audit Area	Auditors' Primary Checks	Suggested System Support
Stationery	➢ Physical Verification of Stationery and confirmation of Balance as per CBS	**Finacle:** ➢ "**ISRA**" – Inventory Status Report ***(Location wise viz., Dual Lock, Individual, Cancelled etc.)*** **BaNCS:** ➢ Through Valuable Paper Inventory System [VPIS] module
Office Accounts (Suspense, Sundry etc.)	➢ Outstanding entries for reporting ➢ Entries outstanding – Whether any provisioning is required?	**Finacle:** ➢ "**IOT**" – Inquire on Transaction (As on date Inquiry) ➢ "**MSGOIRP**" – Outstanding Items Report **BaNCS:** ➢ Through offline reports viz. "Audit BGL accounts age wise break up" and "GL-Outstanding-Accounts" report.
Office Accounts (Suspense, Sundry etc.)	➢ Printing of Office Accounts	**Finacle:** ➢ "**ACLPOA**" – Account Ledger printing Office Account **BaNCS:** ➢ BGL Accounting Menu
Inter Branch Account	➢ Un-reconciled transactions	**Finacle:** ➢ Through Outstanding IBR Report.

Audit Activity / Process / Audit Area	Auditors' Primary Checks	Suggested System Support
		BaNCS: ➢ Through offline "Outstanding IBR Report"/ "IBR Summary report"
TDS Related	➢ TDS Information and Reports	**Finacle:** ➢ "TDSIP" – TDS Inquiry & Reports ➢ Month-end report on account wise / transaction wise Tax deduction. ➢ Bank specific customized Menu / report **BaNCS:** ➢ Through offline monthly report on account wise / transaction wise Tax deduction.

List of Important Menu Commands

2.39 Following is the list of various important menu commands for concurrent auditors based on area of operations in the bank:

(i) Accounts, Customer Master and Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	CUMM / CUMI	Customer Master Maintenance / Inquiry	Inquiry
Finacle 7	ACM / ACI	Account Master Maintenance / Inquiry	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	ACLI	Account Ledger Inquiry	Inquiry
Finacle 7	ACCBAL	Component of Account Balance Inquiry	Inquiry
Finacle 7	ACS	Account Criterion Search	Inquiry (Search / Criterion based)
Finacle 7	CUS	Customer Selection / Inquiry	Inquiry (Search / Criterion based)
Finacle 7	ACINT	Interest Run for Accounts	Inquiry / Report
Finacle 7	INTTM	Interest Table Master Maintenance	Inquiry
Finacle 7	AFI	Audit File Inquiry	Inquiry
Finacle 10	CRM Module	Customer Master maintenance	Inquiry & Modifications
Finacle 10	HACLI, HACLINQ	Account Ledger Inquiry	Inquiry
Finacle 10	HACM, HACMTD	Account Master, Account Master Term Deposits	Inquiry
Finacle 10	HINTTM	Interest Table Master Maintenance	Inquiry
Finacle 10	HAFI	Audit File Inquiry	Inquiry
BaNCS	Customer Management → Enquiries → Search by CIF Number	To verify all accounts of one Customer	Inquiry
BaNCS	Customer Management → Enquiries → Search by ID Number	Search using available information (ID Number)	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
BaNCS	Customer Management ➔ Enquiries ➔ Search by Name	Search using available information (Name)	Inquiry
BaNCS	Customer Management ➔ Relationship / Ownership ➔ Associated Accounts	Inquiry on Linked Accounts, Owned Accounts etc.	Inquiry
Flex Cube	CH021	Account Master Maintenance	Inqiry
Flex Cube	CH701	Customer account balances-Other than loans-For standard accounts but including CC limit accounts	Inquiry
Flex Cube	CH703	RD account balances-Customer wise	Inquiry
Flex Cube	2000	CTI Customer Search	Inquiry
Flex Cube	7004	Customer Name and Address Inquiry	Inquiry
Flex Cube	7100	All Balance Inquiry	Inquiry
Flex Cube	7105	Display Customer Image	Inquiry
Flex Cube	BA095	Account Level Attributes Inquiry	Inquiry
Flex Cube	7002	Balance Inquiry	Inquiry
Flex Cube	CH031	Statement Inquiry	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Flex Cube	BAM24	Account Status Audit Trail Inquiry	Inquiry
Flex Cube	1337	Term Deposit Interest Payout Inquiry	Inquiry
Flex Cube	7020	TERM DEPOSIT Balance Inquiry	Inquiry
Flex Cube	TD023	TERM DEPOSIT Rates History Inquiry	Inquiry
Flex Cube	TD031	TERM DEPOSIT Audit Trail Inquiry	Inquiry
Flex Cube	TD037	TERM DEPOSIT Account Ledger Inquiry	Inquiry
Flex Cube	TD050	TERM DEPOSIT Interest Inquiry	Inquiry
Flex Cube	TD11	TDS Inquiry	Inquiry

(ii) Transactions

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	TM / TI	Transaction Maintenance / Inquiry	Inquiry
Finacle 7	FTI	Financial Transaction Inquiry	Inquiry (Search / Criterion based)
Finacle 7	FTR	Financial Transaction Inquiry Report	Report

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HTI	Transaction Maintenance / Inquiry	Inquiry
Finacle 10	HFTI	Financial Transaction Inquiry	Inquiry (Search / Criterion based)
BaNCS	Deposit / CC / OD Accounts & Services ➔ Enquiries ➔ Transaction	Transaction Enquiry (Additional options available: Transaction Types: 99 – All Financial, 98 – Cash Transaction, 25 – Repayment Details, 33 – Message Details	Inquiry
BaNCS	➔ Branch Accounting (BGL) ➔ Enquire ➔ Transaction	BGL Transaction Enquiry	Inquiry
Flex Cube	TD044	TD Transactions Inquiry	Inquiry
Flex Cube	LN058	Loan Interest Adjustment Transaction	Inquiry
Flex Cube	PM025	Payment Transaction Inquiry	Inquiry
Flex Cube	GLM04	GL Transactions and Movements Inquiry	Inquiry
Flex Cube	AT002	Audit Trail Financial Transactions Inquiry	Inquiry
Flex Cube	BA777	Audit Trail Inquiry for Non-Financial Txns	Inquiry

(iii) Clearing Transactions

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	MCLZOH	Maintain Clearing Zone	Inquiry
Finacle 7	OCTM	Outward Clearing Transaction Maintenance	Inquiry
Finacle 7	ICTM	Inward Clearing Transaction Maintenance	Inquiry
Finacle 10	HOCTM	Maintain Clearing Zone	Inquiry
Finacle 10	HICTM	Outward Clearing Transaction Maintenance	Inquiry
Finacle 10	HMCLZOH	Inward Clearing Transaction Maintenance	Inquiry
BaNCS	**Collection and Cheque Purchase ➔ Enquiries ➔ Enquiries**	Inquiry for Cheque Purchase / on Collection	Inquiry
Flex Cube	ST023	Outward Clearing	Inquiry
Flex Cube	ST033	Inward Clearing	Inquiry
Flex Cube	BA990	Clearing Inquiry	Inquiry
Flex Cube	ST002	Value Date Clearing Inquiry	Inquiry

(iv) Office Accounts Maintenance

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	ACLPOA	Account Ledger Print Office Account	Report
Finacle 7	IOT	Inquire on Transaction	Inquiry & Report

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	MSGOIRP	Outstanding Items Report	Report
Finacle 10	HIOT	Inquire on Transaction	Inquiry & Report
Finacle 10	HACLPOA	Account Ledger Print Office Account	Report
BaNCS	→ Branch Accounting (BGL) → Enquire → Account	Enquiry on BGL Account	Inquiry
BaNCS	→ Branch Accounting (BGL) → Enquire → Account Number Search	Search an Account Number by BGL Name	Inquiry
BaNCS	→ Branch Accounting (BGL) → Enquire → Transaction	BGL Transaction Enquiry	Inquiry
Flex Cube	GLM01	GL Voucher Entry	Inquiry
Flex Cube	GLM02	Chart of Accounts	Inquiry
Flex Cube	GLM04	GL Transactions and Movement Inquiry	Inquiry
Flex Cube	1005	Miscellaneous GL Transfer (Dr/Cr)	Inquiry

(v) **Loans & Advances**

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	SRM	Security Register Maintenance	Inquiry
Finacle 7	HCLM / CLL	Collateral Maintenance	Inquiry
Finacle 7	ACHLM	Account History Limit Maintenance	Inquiry
Finacle 7	ALM	Account Lien Maintenance	Inquiry
Finacle 7	ACTODM	Account TOD Maintenance	Inquiry
Finacle 7	TODRP	TOD Register Printing	Inquiry
Finacle 7	PSP	Pass Sheet Print	Report
Finacle 7	ACLPCA	Account Ledger Printing	Report
Finacle 7	LAGI	Loan General Inquiry	Inquiry (Criterion based search)
Finacle 7	LAOPI	Loan Overdue Position Inquiry	Inquiry (Criterion based search)
Finacle 7	LTL	Limit Tree Lookup	Inquiry
Finacle 7	LNDI	Limit Node Inquiry	Inquiry
Finacle 7	AINTRPT	Interest Report for Accounts	Report
Finacle 10	HSCLM	Security Register Maintenance	Inquiry
Finacle 10	HALM	Account Lien Maintenance	Inquiry
Finacle 10	HACTODM	Account TOD Maintenance	Inquiry
Finacle 10	HPSP	Pass Sheet Print	Report
Finacle 10	HACLHM	Account Limit History Maintenance	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HAINTRPT	Interest Report for Accounts	Report
Finacle 10	HINTPRF	Interest Proof Report	Report
BaNCS	Deposit / CC / OD Accounts & Services → Enquiries → Deposit / CC / OD Account	To verify the Account Master Details	Inquiry
BaNCS	Deposit / CC / OD Accounts & Services → Enquiries → Statement Print	Printing Statement of Account for a Deposit or CC / OD	Report
BaNCS	Deposit / CC / OD Accounts & Services → Enquiries → Short	Basic details on Enquiry on Screen on Deposit Accounts	Inquiry
BaNCS	Deposit / CC / OD Accounts & Services → Enquiries → Long	Additional Details on Enquiry Screen for Deposit Accounts	Inquiry
BaNCS	Deposit / CC / OD Accounts & Services →Interest Rate History	Details of changes in Interest Rate for an account	Inquiry
BaNCS	→ DL/TL Accounts & Services → Loan Tracking → Operations	Loan account operations	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
BaNCS	→ DL/TL Accounts & Services → Loan Processing → Generate Repayment Schedules → Action – "E"	To print Repayment schedule for a DL / TL Account	Report
BaNCS	→ DL/TL Accounts & Services → Enquiries → Short → Option "Balance Breakup Enquiry"	To view amount of Arrears & Breakup of Principal, Interest Realized, Charges & Arrear of Interest	Inquiry
BaNCS	→ DL/TL Accounts & Services → Security (Primary / Collateral) → Customer → Enquiry → Enquire Security Summary	Enquire on linked collateral	Inquiry
Flex Cube	CH066	Limit Collateral Inquiry	Inquiry
Flex Cube	CHM06	OD Collateral Maintenance	Inquiry
Flex Cube	CHM07	OD Limit Master Maintenance	Inquiry
Flex Cube	ST070	Cheque Purchase	Inquiry
Flex Cube	CH033	Average Quarterly / Monthly Balance Inquiry	Inquiry
Flex Cube	TDM24	Lien Master	Inquiry
Flex Cube	1413	Loan Disbursement Inquiry	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Flex Cube	LN522	Account Schedule Inquiry	Inquiry
Flex Cube	LNM10	Account Transactions Inquiry	Inquiry
Flex Cube	BA433	Collateral To Accounts Inquiry	Inquiry
Flex Cube	BA434	Account To Collateral Inquiry	Inquiry

(vi) DD / PO, Cheque Book maintenance, Stop Payments and Security Stationery maintenance

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	DDSM	DD Status Maintenance	Inquiry
Finacle 7	DDIP	Inquiry on Specific DD Paid	Inquiry
Finacle 7	ISRA	Inventory Status Report	Report
Finacle 7	IMI	Inventory Movement Inquiry	Inquiry
Finacle 7	ICHB	Issue Cheque Book	Inquiry
Finacle 7	CHBM	Cheque Book Maintenance	Inquiry
Finacle 7	SPP	Stop Payment of Cheque	Inquiry
Finacle 7	SPRG	Stop Payment Register	Report
Finacle 10	HDDSM	DD Status Maintenance	Inquiry
Finacle 10	HDDIP	Inquiry on Specific DD Paid	Inquiry
Finacle 10	HISRA	Inventory Status Report	Report
Finacle 10	HIMI	Inventory Movement Inquiry	Inquiry
Finacle 10	HICHB	Issue Cheque Book	Inquiry
Finacle 10	HCHBM	Cheque Book Maintenance	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 10	HSPP	Stop Payment of Cheque	Inquiry
Finacle 10	HSPRG	Stop Payment Register	Inquiry
BaNCS	➔ Valuable Paper Inventory System [VPIS] ➔ Enquiry of VPIS ➔ General Enquiry	To check inventory status	Inquiry
BaNCS	➔ VPIS ➔ Lost / Damaged / Cancelled Inventories	Location for Lost / Damaged / Cancelled Inventories	Inquiry
BaNCS	➔ VPIS ➔ Enquiry of VPIS ➔Teller Level Inquiry	Details of Inventory available at Teller level	Inquiry
Flex Cube	CH078	Cheque Status Maintenance	Inquiry
Flex Cube	CHM35	Stop Cheque Instructions	Inquiry
Flex Cube	CHM37	Cheque Book Issue Maintenance	Inquiry
Flex Cube	IV011	Stock Inquiry	Inquiry
Flex Cube	IV004	Inventory Lost report Register maintenance	Inquiry
Flex Cube	MCA80	Inquiry of sold/issued inventory	Inquiry

(vii) Compliances

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	TDSIP	TDS Inquiry / Print	Inquiry and Report
Finacle 7	AFSM	Account Freeze Maintenance	Inquiry
Finacle 10	HTDSIP	TDS Inquiry / Print	Inquiry and Report
Finacle 10	HAFSM	Account Freeze Maintenance	Inquiry
Flex Cube	TDS06	Tax Parameters Maintenance	Inquiry
Flex Cube	TDS04	Tax waiver criteria Maintenance	Inquiry
Flex Cube	TDS05	Customer special Tax code maintenance	Inquiry
Flex Cube	TDS11	Tax Inquiry	Inquiry

(viii) Trade Finance and Foreign Exchange Transactions

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	INBOEM	Bill of Entry Maintenance	Inquiry
Finacle 7	BI	Bills Inquiry (Inland)	Inquiry (Criterion based search)
Finacle 7	BP	Bills Inquiry (Inland) – Printing	Report
Finacle 7	BM	Bill Maintenance (Inland)	Inquiry
Finacle 7	FBI	Foreign Bill Inquiry	Inquiry (Criterion based search)
Finacle 7	FBM	Foreign Bill Maintenance	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Finacle 7	FBP	Foreign Bill Inquiry – Printing	Report
Finacle 7	BRBPR	Balancing Report for Bills Purchased (Inland)	Report
Finacle 7	BRCR	Balancing Report for Bills on Collection (Inland)	Report
Finacle 7	FBBR	Balancing Report for Foreign Bills	Report
Finacle 7	DCQRY	Documentary Credit Query	Inquiry (Criterion based search)
Finacle 7	GI	Guarantee Inquiry	Inquiry
Finacle 7	IRM	Inward Remittance Maintenance	Inquiry
Finacle 7	ORM	Outward Remittance Maintenance	Inquiry
Finacle 10	HINBOEM	Bill of Entry Maintenance	Inquiry
Finacle 10	MIIB	Maintain Import & Inward Bills	Inquiry
Finacle 10	MEOB	Maintain Export & Outward Bills	Inquiry
Finacle 10	IBL	Bill Inquiry	Inquiry (Criterion based search)
Finacle 10	HBRBPR	Balancing Report for Bills Purchased (Inland)	Inquiry
Finacle 10	HBRCR	Balancing Report for Bills on Collection (Inland)	Inquiry
Finacle 10	HFBBR	Balancing Report for Foreign Bills	Inquiry
Finacle 10	HGI	Guarantee Inquiry	Inquiry
Finacle 10	HIRM	Inward Remittance Maintenance	Inquiry
Finacle 10	HORM	Outward Remittance Maintenance	Inquiry

CBS Package	Menu Code / Access path	Menu Name	Menu Type (Inquiry / Report)
Flex Cube	SY001	Guarantee Inquiry	Inquiry
Flex Cube	BIM04	Bill Parameters Maintenance	Inquiry
Flex Cube	BIM05	Bills Processing Maintenance	Inquiry
Flex Cube	BI001	Bills Data Entry	Inquiry

Note:

The discussion of Menu codes / commands in this chapter is only for guidance of members. The purpose of inclusion of the same here is to understand functioning of banking software. Moreover, with the continuous changes and customization requests by banks, all the menu codes may not be available / accessible in all the banks.

The Finacle menu codes discussed in this chapter is for version 7 (except expressly mentioned). Finacle has introduced new version namely Finacle 10.X. Few banks have already migrated to newer version and few more are in process of migration. Under Finacle 10.X there are changes in Menu Codes apart from other navigational changes.

Disclaimer:

Images, Logo, Screen Shots, Menu Codes, Software Name, etc., are the property of respective Software developer/ Trademark owners.

Concurrent Auditing Techniques

2.40 Concurrent Auditing Techniques are as follows:

- Integrated Test Facility (ITF)
- Snapshots
- Extended Record Technique
- System Control Audit Review File (SCARF)
- Continuous and Intermittent Simulation (CIS)

Integrated Test Facility (ITF)

2.41 An integrated test facility (ITF) creates a fictitious entity in a database to process test transactions simultaneously with live input. It can be used to incorporate test transactions into a normal production run of a system. It is a test using simulated transactions and dummy master records within a client's master file so that test data are processed simultaneously with actual input. The objective is to substantiate control reliability.

Problem with using ITF is that it affects the output of the application system. Therefore, it is important that effects of ITF transactions should be removed by the application software prior to producing output. One can follow either of the under mentioned:

- Modify application program to ignore their effects while preparing outputs
- Submit additional inputs for removing their effects.
- Submit trivial entries as test data so that their effect on the output is minimal.

Snapshots

2.42 In computer systems, a snapshot is the state of a system at a particular point in time. The term was coined as an analogy to that in photography. It can refer to an actual copy of the state of a system or to a capability provided by certain systems. An embedded audit module can be used to take pictures of a transaction. The snapshots can either be printed immediately or saved to a file for later printing.

Auditors need to determine:

- Where to take snapshots
- Which transactions will be subject to snapshot
- How and when the snapshot data will be presented for evaluation

Extended Record Technique is a modification of the Snapshot technique. Where a Snapshot technique involves writing a record for each snapshot point and Snapshots are usually stored where it is taken, extended record technique appends data for each snapshot point to a single record. Thus, all data relating to a transaction is kept in one place.

System Control Audit Review File (SCARF)

2.43 SCARF is the most complex of all the techniques as it involves embedding audit modules in an application system to provide continuous monitoring of a system's transactions.

Embedded audit modules are placed at pre-determined points to gather information about transactions or events that auditors deem to be material. Data collected via these routines includes errors and irregularities, policy and procedural variances, system exceptions, statistical samples, snapshots, etc.

- Information collected is written to a special SCARF file.
- Auditor's then examine the information contained on this file.

Continuous and Intermittent Simulation (CIS)

2.44 This is a variation of SCARF continuous audit technique. It is used to trap exceptions whenever the application system uses a DBMS. During application system processing, CIS executes in the following way:

(i) DBMS reads a transaction. It is passed to CIS. CIS then determines whether it wants to examine the transaction further. If yes, the nest steps are performed, otherwise it waits to receive further data from DBMS.

(ii) CIS replicates the application system's processing.

(iii) Result of application system processing and CIS processing are compared.

(iv) Data about discrepancies are written to a special audit file.

(v) If discrepancies are material, CIS can instruct DBMS to reject updates.

Advantage

2.45 CIS does not require modification to the application system (DBMS needs to be modified to trap CIS transactions).

Disadvantage

2.46 It cannot collect evidence at processing points other than DBMS.

Chapter 3
Revenue Audit

3.1 Revenue audit is the audit of items governing income and expenditure of banks. Basically, this type of audit is conducted with a view to verify the accuracy and relevance of expenditure incurred and income earned by the banks according to applicable latest circular and notification. Auditor is only required to concentrate on the areas which affect revenue items of the bank.

3.2 Normal procedure to conduct the revenue audit is as under:

(i) Before commencing the revenue audit, the auditors are required to collect the list of auto levy (system levy) charges and manual levy of charges.

(ii) Study the relevant circulars pertaining to charges given by the bank. Go through the format of audit report and annexure attached to the audit report.

(iii) Prepare a separate file for audit and don't forget to carry audit engagement letter given by the appointing authority.

(iv) Prepare the audit programme for all major areas to be covered.

(v) Auditors are advised to keep in mind the period of audit to set up schedule for audit, so as to ensure adequate and appropriate coverage and timely completion.

(vi) Go through the previous revenue audit reports and concurrent audit reports of branch to get the overview of possible nature of leakage.

(vii) Obtain some basic view about branch's banking software so as to facilitate easy viewing of customer ledger.

(viii) Ask the branch to make available Advances Sanction Register for Audit Period.

(ix) With a view to obtain knowledge of accounts, an appropriate sample should be selected of following accounts:

- o Cash Credit Accounts
- o Top Saving Accounts

- o Top Current Accounts
- o Top Term Deposit Accounts
- o Overdue advances in audit period
- o Premature Fixed Deposit Receipts (FDRs)
- o List of NPA Accounts of branch and recoveries made during the period to be, appropriately, adjusted against interest/ instalment.

Income of Bank

3.3 List of areas to be covered for Income head and procedure for its audit are as under:

(a) Interest earned on advances

(i) Check whether interest has been charged in accordance with applicable circulars of the bank.

(ii) Check interest calculation on selective basis.

(iii) Check whether interest has been charged as per adhoc/ special sanction letter.

(iv) Check that revised interest rates are properly applied in system from relevant date of applicability.

(b) Penal interest on overdue instalments and on late submission of Stock Statement/ Quarterly Monitoring Data (QMD)

Generally, penal interest is to be charged 1% subject to maximum of 2%. Such panel interest is charged in following circumstances:

(i) Instalment is overdue.

(ii) Amount exceeds the drawing power.

(iii) Delay in submission of stock statement.

(iv) Delay in submission of Quarterly Monitoring Data (QMD)/ Financial Statements.

(v) Delay in renewal of working capital limits.

(c) CIBIL charges

Check whether CIBIL charges are properly debited as per circular of charges.

(d) Processing fees

Processing fees is to be recovered on advances, as per sanction during audit period, wherever applicable as per circulars of charges, such as. Term loans, *viz.*, housing loans, personal loans, vehicle loans

Cash Credits and overdrafts

Bank Guarantee/Letter of Credit/ Buyer's Credit

Other Demand Loans

(e) Cash credit renewal charges

Cash Credit Limit should be renewed every year as per the terms and conditions of the bank. Verify the renewal register whether every cash credit account has been debited by cash credit renewal charges/ extension charges.

(f) Inspection charges

Verify that the charges are properly debited in borrower's ledger as per circular of charges.

(g) Documentation charges

Documentation charges should be debited in each sanction during the audit period as per the circular of charges.

(h) Minimum balance charges

- These charges are, generally, debited on saving accounts/ current accounts and debited by data centre in case of CBS branches.
- Verify some account on random basis that these charges are properly debited in accounts as per applicable circulars if account balance falls below minimum.

(i) Ledger folio charges

- These charges are to be charged to current accounts and cash credit accounts on basis of per ledger folio.
- Generally, these charges are debited by data centre in case of CBS Branches, so selective accounts should be checked to determine whether charges are debited as per circulars.

(j) Cash recovery against NPA Accounts

Confirm that all outstanding charges, interest outstanding are adjusted against such recoveries, then only principal amount of loan is adjusted.

(k) Locker rent Charges

Generally, locker rent register is maintained by the bank and applicable charges are debited to saving account of customer. Auditors have to check out whether charges as per circular have been debited to customer or not. However, it is to be noted that locker rent charges is not part of revenue leakage.

(l) DD commission, IBC/ OBC commission, cheque book charges, stop payment charges

- Obtain Pay order, DD register, IBC/OBC register from the branch and verify on selective basis that charges are properly debited to customer's account.
- Obtain cheque book register and verify that series of cheque books are properly entered in register. When cheque book is issued to customer check series fed into the system so that cheque book charges are debited to customer's ledger.
- Stop payment charges are debited on basis of per instrument basis (no of instrument* rate per instrument).

(m) Income From Investment

- Verify whether any investments have been made by the branch.
- Obtain investment register from branch and verify whether interest and dividend are timely collected and accounted by the bank as per applicable rates.

(n) Commitment charges for the facilities not utilised/ short utilised

Many banks have started levying penal interest for short utilisation/ non-utilisation of cash credit/ term loan facility. Revenue auditors are required to check the bank policy on levying such charges and accordingly, verify the same with the statement of accounts.

Expenses of Bank

3.4 Following are the major heads to be verified by the auditor related to expenses of bank:

(a) Interest paid on deposit accounts

Generally, banks give credit of interest to customer's account on half yearly/ quarterly basis by giving command of Interest Credit in case of CBS Operation. Auditor has to check on selective basis whether interest has been credited on due time and at appropriate rate as per the applicable circulars.

(b) *Interest on term deposits*

- Whether the rates fed in the system are as per policy of the bank.
- In case of premature repayment of deposit, applicable penalty and reduced rate of interest has been charged.
- If a term deposit matures and proceeds are unpaid, the amount left unclaimed with the bank shall attract rate of interest as applicable to saving account.

(c) General branch expenses

General branch expenses are as per delegated power on respective accounts.

(d) Legal/ valuation charges

Legal/ valuation charges on non-performing accounts are as per schedule of charges.

Chapter 4
Stock and Book Debt Audit

Introduction

4.1 Working capital finance in the form of cash credit against the security of hypothecation of stock and debtors is one of the most common modes of finance, frequently adopted by various bankers. The borrowers in such cases are expected to submit the details of stock and debtors every month on the basis of which Drawing Power is calculated by the banks after reducing the prescribed margin. Bankers for ascertaining the genuineness and correctness of Stock and Debtors statements appoint chartered accountant firms at frequent intervals to conduct stock audit in eligible cases.

Appointment of Stock Auditors and Period of Audit

4.2 The appointment of stock auditors is, generally, made by the regional or zonal offices. Terms of appointment are prescribed by such offices which sometimes involves conducting of stock audit as one-time exercise only while in others it may be a contract for two half yearly visits during a particular financial year, of which first visit to be conducted before September and second visit before March. The stock audit involves audit of latest stock and debtor's information of the borrower and the report should give the position of stock and debtors ideally on the date of visit. Further, it will also make examination of past data submitted by the borrower to the bank and appearing in the books of accounts of the borrower, to check reliability of information submitted by the borrower.

Objectives of Stock Audit

4.3 The banker appointing the chartered accountant firm for conducting stock audit has main objective of ascertaining whether the security (borrower's stock and debtors) against which finance has been made is safe and is valued correctly.

The various purposes expected to be achieved through stock audit may be summarized as follows:

- Ensure proper storage and handling of stock;
- Identify whether there exist any slow moving and non-moving or obsolete stock and if yes, whether it has been segregated or valued accordingly;
- Verify whether the stock is adequately insured against fire and other natural calamities (in appropriate cases against other risks like theft, burglary, marine, riots, etc. as per sanction);
- Ascertain whether physical stock tally with the stock statement submitted to the banker;
- Ascertain whether hypothecated stock is realizable;
- Confirm that stock is owned by the borrower and finance is made against value of paid stock only;
- Examine the age wise debtors outstanding as per books and as per statement submitted by the bank, steps taken for recovery of long pending debtors and likely instances of debtors turning bad, if any.

Steps involved in Stock Audit

4.4 Stock audit is necessarily required to be conducted at the borrowers place for abovementioned purposes. However, before visiting the borrower, understanding of the entity, it's banking operations and financial affairs is must. Therefore, it is advisable to visit the respective branch where the borrower is having the account so as to gather the information relating to sanction, account operations, nature of business, performance of the borrower and other fundamental information along with the observations noted by Internal Inspectors, Concurrent Auditors, etc., to have a brief understanding about the borrower and its financial affairs.

4.5 Following are the major steps involved in stock audit:

(i) Visit to Borrower's Branch

Banks, generally, have the system of maintaining two folders (in few cases only one folder) for each borrower of which one is used for keeping original documents (viz., Demand Promissory Note, Hypothecation Deed, Guarantee Bond, etc.) while other folder contains application form, project report, sanction letter, audited financial statements, previous stock audit report, etc. Stock statements submitted each month by the borrower are kept either with the correspondence file or may be kept in a single file meant for keeping stock statements of all the borrowers. Scrutiny of both the files along with the account operations and DP Register with reference to terms of sanction helps stock auditor to gain insight about the borrower' affairs and conduct of the account.

(ii) Visit to Borrower and Verification of Stock

Once the basic information is collected from the bank branch, it is time to visit the borrower. It is advisable to carry audit questionnaire at the time of visit so that no important point / area is missed out. Visit to borrower involves verification of stock and debtors, inquiry about MIS and internal control, future projections and financial plans of the borrower and analysis of past results and bank operations.

(iii) Preparation of Audit Report and Discussion About Audit Findings

After conclusion of visits, stock audit report in the prescribed format, if available, is to be prepared. In the absence of format, questionnaire prepared can itself also act as a report format. However, at the end of the questionnaire or in the covering letter itself (where auditor has to report in bank specified format) summary of major adverse findings or points for future action must be submitted by the auditor. Before submission of audit report, discussion about audit findings with the monitoring branch as well as borrower may be a good practice which may bring further clarity in reporting.

Common Irregularities/ Observations in Stock Audit

4.6 The common irregularities that may be observed by the chartered accountant firm during stock audit can be summarized as follows:

(i) Observations about statement submission and scrutiny

- Stock/ book debt statements not submitted or not submitted on time
- Inadequate details, viz., rate, quantity and amount of different type of stock items not stated in the statement
- Scrutiny of stock statements not done

- DP Register not written up to date
- Age-wise analysis of debtors not given/ done. Debtors over 90 days (or as per sanction) considered for drawing power
- Drawing power not correctly calculated
- Latest visit report by branch official not on record

(ii) Observations about account operations

- Operations in the accounts not scrutinized with reference to projections, QIS statements, audited accounts, etc.,
- Defects pointed out by the Internal Auditors/ Inspectors/ Concurrent Auditors not complied with
- No review or delay in review of renewal of account
- All sales as per financial statements not routed through account
- Cash withdrawal during current period is abnormal
- Frequent overdrawing in the account

(iii) Observations about Insurance coverage

- Under insurance of stock
- Insurance expired but not renewed
- Premium for renewal policy paid but policy not held on record
- Insurance Policy without Bank Clause
- No coverage of all the risks as per sanction
- Wrong description of goods on insurance policy
- Location of goods wrongly stated
- All locations of stock not covered
- All items specified in sanction letter for computation of DP are not covered

(iv) Observations about verification of Stock and Creditors

- Stock register not maintained/ updated
- Obsolete stock not excluded from stock figures submitted to banks
- Deteriorating stock turnover ratio

- Stock figures submitted at the year end and as per financial statement not matching
- Stock/ debtors as per statements submitted not matching with books
- Confirmation for inventory with third party not obtained or physical verification of inventory not done
- Material received from third parties for job work not excluded while calculating drawing power
- Trade creditors are to be excluded

(v) Observations about verification of Sundry debtors

- Existence of long pending debtors
- Long pending debtors had shown as below 90 days debts to bank
- Increase in the average collection period of debtors
- Dispute with debtors and pending court cases
- Amount receivable from sister concern considered for calculation of drawing power
- Advances received from debtors not reported resulting into lower DP than calculated by bank

(vi) Other General Observations

- Diversion of funds and inter account transfers are not properly monitored
- Borrower having operations with other bank for which permission of lender not obtained
- Bank name plate not displayed

Above list is illustrative only and not the exhaustive one. In actual practice, there may be other observations / irregularities over and above stated in the list.

Reporting on Stock Audit

4.7 The auditor may consider the following points while reporting on stock audit:

(i) The report has to be submitted to the authority appointing the auditor.

(ii) It should be in the prescribed format and should be exhaustive and inclusive of all facts and summaries.

(iii) It should include the date, time, location of visit and the name of the officials conducting the audit and the official of the entity present at the entity at the time of conducting the audit.

(iv) Copies of confirmations, management representations, etc., should be submitted along with the report.

(v) If the auditor is unable to obtain sufficient appropriate audit evidence concerning the existence of Inventories or adequacy of procedures adopted by the management in respect of physical inventories count, the auditor should make a reference to a scope of limitation in his audit report.

(vi) If the inventories is not disclosed appropriately in the financial statements, the auditor should issue a qualified opinion.

Special Considerations while conducting Stock Audit

4.8 Following should be also considered while conducting stock audit:

(i) If the stock statement as shown in the hypothecation statement does not tally with the stocks as in the balance sheet, then appropriate action should be taken to find reasons for the differences.

(ii) It should be seen that the stocks have been properly valued.

(iii) It should be seen that current assets are not over-stated.

(iv) It should be seen that the turnover is not over-stated.

(v) It should be seen that the stocks that are genuinely owned by the borrower are shown in the accounts.

Appendices

APPENDIX I

Concurrent Audit System in Commercial Banks - Revision of RBI's Guidelines

RBI/2015-16/133

DBS.CO.ARS.No. BC. 2/08.91.021/2015-16

July 16, 2015

The Chairman & Managing

Director/ Chief Executive Officers

of all Scheduled Commercial Banks

(other than Regional Rural Banks)

Dear Sir

Concurrent Audit System in Commercial Banks - Revision of RBI's Guidelines

As you are aware, guidelines on 'concurrent audit system in commercial banks' were issued by us vide our circular DOS.No.BC.16/08.91.021/96 dated August 14, 1996 setting out the scope and coverage of concurrent audit system in commercial banks.

In view of the changes since then in banks' organizational structure, business models, use of technology (implementation of Core Banking Solution), etc., a need was felt to have a relook at the concurrent audit system in the banking sector. Accordingly, the existing guidelines have been revised which are set out in Annex I.

2. Since the concurrent audit system is regarded as part of a bank's early warning system to ensure timely detection of irregularities and lapses, which also helps in preventing fraudulent transactions at branches, the bank's management may continue to bestow serious attention to the implementation of various aspects of the system such as selection of branches/coverage of business operations, appointment of auditors, appropriate reporting procedures, follow-up/rectification processes and utilization of the feedback from the system for appropriate and quick management decisions.

3. You may ensure that, based on the revised guidelines indicated in Annex I, a review of the present system of concurrent audit is carried out immediately and necessary changes are incorporated therein. The modified concurrent audit system of your bank should be placed before the Audit Committee of Board of Directors (ACB).

4. The bank should, once in a year, review the effectiveness of the system and take necessary measures to correct the lacunae in the implementation of the Programme.

Yours faithfully

(Indrani Banerjee)

Chief General Manager
Encl: As above

ANNEXURE I

Revised Guidelines for Concurrent Audit System in Commercial Banks

(A) Scope of concurrent audit

Concurrent audit is an examination which is contemporaneous with the occurrence of transactions or is carried out as near thereto as possible. It attempts to shorten the interval between a transaction and its examination by an independent person. There is an emphasis in favour of substantive checking in key areas rather than test checking. This audit is essentially a management process integral to the establishment of sound internal accounting functions and effective controls and setting the tone for a vigilant internal audit to preclude the incidence of serious errors and fraudulent manipulations.

A concurrent auditor may not sit in judgment of the decisions taken by a branch manager or an authorized official. This is beyond the scope of concurrent audit. However, the audit will necessarily have to see whether the transactions or decisions are within the policy parameters laid down by the Head Office, they do not violate the instructions or policy prescriptions of the RBI, and that they are within the delegated authority.

In very large branches, which have different divisions dealing with specific activities, concurrent audit is a means to the in-charge of the branch to ensure on an ongoing basis that the different divisions function within laid down parameters and procedures.

(B) Coverage of business/branches

In view of significant developments in the banking sector during the past decade, it is required that new areas posing risk may be brought under the purview of concurrent audit. A large number of activities / operations are being carried out in a centralized manner at various units set up for that purpose and the scale of transactions / operations undertaken at these units is large. With a view to ensuring that the functioning of these units is as per the internal as well as regulatory guidelines and mitigating the risk associated with large-scale operations, such non-branch units may be brought under the purview of concurrent audit.

While selecting the branches for concurrent Audit, the risk profile of the branches needs to be considered. The branches with high risk are to be subjected to concurrent audit irrespective of their business size. Further, all specialized branches viz., Agri, SME, Corporate, Retail Assets, Portfolio Management, Treasury, Forex, Back Office, etc., may be covered under concurrent audit. Certain areas where risk has reduced on account of computerization, implementation of core banking system may be excluded from the purview of concurrent audit.

Concurrent audit at branches should cover at least 50% of the advances and 50% of deposits of a bank. The following branches, business activities/verticals of a bank may be subject to concurrent audit:

Branches rated as high risk or above in the last Risk Based Internal Audit (RBIA) or serious deficiencies found in Internal Audit.

All specialized branches like Large Corporate, Mid Corporate, exceptionally large/very large branches (ELBs/VLBs), SME.

All Centralized Processing Units like Loan Processing Units (LPUs), service branches, centralized account opening divisions, etc.

Any specialized activities such as wealth management, portfolio management services, Card Products Division, etc.

Data Centers.

Treasury/branches handling foreign exchange business, investment banking, etc. and bigger overseas branches.

Critical Head Office Departments.

Any other branches or departments where, in the opinion of the bank, concurrent audit is desirable.

(C) Types of activities to be covered

(1) The main role of concurrent audit is to supplement the efforts of the bank in carrying out simultaneous internal check of the

transactions and other verifications and compliance with the procedures laid down.

(2) The scope of concurrent audit should be wide enough/focused to cover certain fraud prone areas such as handling of cash, deposits, advances, foreign exchange business, off balance sheet items, credit-card business, internet banking, etc.

(3) The detailed scope of the concurrent audit should be clearly and uniformly determined for the bank as a whole by the bank's Inspection and Audit Department in consultation with the bank's Audit Committee of the Board of Directors (ACB).

(4) In determining the scope, importance should be given to checking high-risk transactions having large financial implications as opposed to transactions involving small amounts.

(5) While the detailed scope of concurrent audit may be determined and approved by ACB, certain minimum items of coverage are given in Annex II. In addition to the above, the items where RBI has specifically advised the banks to be covered under concurrent audit, may also be part of the checklist of the concurrent auditor.

(D) Appointment of Auditors and Accountability

(i) The option to consider whether concurrent audit should be done by bank's own staff or external auditors (which may include retired staff of its own bank) is left to the discretion of individual banks.

(ii) In case the bank has engaged its own officials, they should be experienced, well trained and sufficiently senior. The staff engaged in concurrent audit must be independent of the Branch where concurrent audit is conducted.

(iii) Appointment of an external audit firm may be initially for one year and extended upto three years, after which an auditor could be shifted to another branch subject to satisfactory performance.

(iv) If external firms are appointed and any serious acts of omission or commission are noticed in their working, their appointments may be cancelled and the fact may be reported to RBI & ICAI.

(E) Facilities for effective Concurrent Audit

It has been represented that concurrent audit is not often effective because adequate facilities in terms of space, availability of records, etc. are not available. To improve the effectiveness of concurrent audit it is suggested that -

(i) banks arrange for an initial and periodical familiarization process both for the bank's own staff when entrusted with the concurrent audit and for the external auditors appointed for the purpose.

(ii) all relevant internal guidelines/circulars/important references as well as relevant circulars issued by RBI/SEBI and other regulating bodies should be made available to the concurrent auditors on an on-going basis.

where adequate space is not available, concurrent auditors can commence work immediately after the close of banking hours.

(F) Remuneration

Terms of appointment of the external firms of Chartered Accountants for the concurrent audit and their remuneration may be fixed by banks at their discretion. Broad guidelines should be framed by ACB for this purpose. Suitable packages should be fixed by each bank's management in consultation with its ACB, keeping in view various factors such as coverage of areas, quality of work expected, number of people required for the job, number of hours to be spent on the job, etc.

(G) Reporting Systems

(i) The bank may devise a reporting system and periodicity of various check list items as per its sensitivity.

(ii) Minor irregularities pointed out by the concurrent auditors are to be rectified on the spot. Serious irregularities should be straightaway reported to the Controlling Offices/Head Offices for immediate action.

(iii) There should be zone/area-wise reporting of the findings of the concurrent audit to ACB and an annual appraisal/report of the audit system should be placed before the ACB.

(iv) Whenever fraudulent transactions are detected, they should immediately be reported to Inspection & Audit Department (Head Office) as also to the Chief Vigilance Officer as well as Branch Managers concerned (unless the branch manager is involved).

(v) There should be proper reporting of the findings of the concurrent auditors. For this purpose, each bank should prepare a structured format. The major deficiencies/aberrations noticed during audit should be highlighted in a special note and given immediately to the bank's branch controlling offices. A quarterly review containing important features brought out during concurrent audits should be placed before the ACB.

(vi) Follow-up action on the concurrent audit reports should be given high priority by the Controlling Office/Inspection and Audit Department and rectification of the features done without any loss of time.

(vii) Banks are advised to :

(1) review the selection of auditors.

(2) initiate and operate a system for appraisal of the performance of concurrent auditors.

(3) ensure that the work of concurrent auditors is properly documented.

(4) be responsible for the follow-up on audit reports and the presentation of the quarterly review to the ACB.

ANNEXURE II

Minimum Audit Programme for Concurrent Audit System in Commercial Banks

Sr. No.	Items
A	Cash transactions -Verify
(i)	Surprise physical verification of cash at branch and ATM along with safekeeping and custody.
(ii)	Daily cash transactions, particularly any abnormal receipts & payments.
(iii)	Surprise verification of cash by an officer other than the joint custodian.
(iv)	Proper accounting of and availability of insurance cover for inward and outward cash remittances.
(v)	Accounting of currency chest transactions and delays/omission in reporting to RBI.
(vi)	Reporting of Counterfeit Currency.
(vii)	All cash transactions of Rs. 10 lakh and above reported in CTR.
(viii)	That all cash transaction of Rs. 50,000 and above invariably indicate Pan No./Form 60.
B	Clearing transactions -Verify
(i)	Reconciliation with bank's account at Clearing House and review of old outstanding entries for reconciliation.
(ii)	Drawings allowed against uncleared instruments - sanction by the controlling authority.
C	Remittances/Bills for Collection -Verify
(i)	Remittance of funds by way of DDs/TTs/MTs/TC/NEFT/RTGS any other mode in cash exceeding the prescribed limit.
(ii)	Documents of title (lorry receipts, railway receipts, etc.) obtained in favour of the bank and the concerned transporters are on the IBA approved list.

(iii)	Outstanding balance in DP and other transit accounts pending payment beyond prescribed period.
D	Deposits -Verify
(i)	Adherence to KYC/AML guidelines in opening of fresh accounts and monitoring of transactions in such accounts.
(ii)	Large term deposits received and repaid including checking of repayment of term deposit in cash beyond permissible limit.
(iii)	Accounts opened and closed within a short span of time i.e., accounts with quick mortality.
(iv)	Activation and operations in inoperative accounts.
(v)	Value dated transactions.
(vi)	Settlement of claims of deceased customers and payment of TDRs against lost receipts and obtention of indemnities, etc. To check revival of dormant accounts and accounts with minimum activities.
(vii)	Examination of multiple credits to single accounts.
E	Treasury operations -Verify
(i)	If branch has acted within HO instructions for purchase and sale of securities.
(ii)	Periodic confirmation of Derivative contracts with counterparties.
(iii)	Adherence to regulatory guidelines with respect to Treasury deals/structured deals.
(iv)	Controls around deal modification/cancellation/deletion, wherever applicable.
(v)	Cancellation of forward contracts and passing/recovery of exchange gain/loss.
(vi)	Gaps and OPL maintained in different currencies vis-à-vis prescribed limit for the same.
(vii)	Reconciliation of Nostro and Vostro accounts-balances in Nostro accounts in different foreign currencies are within the limits prescribed by the bank.

(viii)	Collection of underlying documents for Derivative & Forward contracts. Delays, if any.
(ix)	Instances of booking and cancellation of forward contracts with the same counterparty within a span of couple of days or a few days.
(x)	Sample check some of the deals and comment on the correctness of computation.
(xi)	Checking of application money, reconciliation of SGL account, compliance to RBI norms.
(xii)	Checking of custody of unused BR Forms & their utilization in terms of Master Circular on Prudential Norms on Classification, Valuation and Operations of Investment Portfolio by banks.
(xiii)	To ensure that the treasury operations of the bank have been conducted in accordance with the instructions issued by the RBI from time to time.
F	Loans & Advances-Verify
(i)	Report Bills/cheques purchased, if in the nature of accommodation bills.
(ii)	Proper follow-up of overdue bills purchased/discounted/negotiated.
(iii)	Fresh loans and advances (including staff advances) have been sanctioned properly and in accordance with delegated authority.
(iv)	Reporting of instances of exceeding delegated powers to controlling/head office by the branch and have been confirmed or ratified by the competent authority.
(v)	Securities and documents have been received as applicable to particular loan.
(vi)	Securities have been properly charged/ registered and valued by competent person. Whether the same has been entered in the bank's system.
(vii)	All conditions of sanction have been complied with.
(viii)	Master data relating to limit, rate of interest, EMI, moratorium period details have been correctly entered and updated/modified in the system.
(ix)	Value dated entries passed in advances accounts.

(x)	Post disbursement supervision and follow-up is proper, such as timely receipt of stock and book debt statements, QIS data, analysis of financial data submitted by borrower, verification of securities by third parties, renewal of limits, insurance, etc.
(xi)	Whether there is any misutilisation of the loans and whether there are instances indicative of diversion of funds.
(xii)	Compliance of prudential norms on income recognition, asset classification and provisioning pertaining to advances.
(xiii)	whether monthly updating of drawing power in the computer system on the basis of stock statements/book debt statement/ other financial data received from the borrowers.
(xiv)	Recovery in compromise cases is in accordance with the terms and conditions of the compromise agreement.
(xv)	To check review and renewal of loans.
G	LC/BG-Verify
(i)	LC/BG issued/amended as per the approved format/model guarantee prescribed and standard limitation clause incorporated. Whether counter indemnity obtained as prescribed.
(ii)	Any deviation from the terms of sanction in regard to margin, security, purpose, period, beneficiary, collection of charges, commission/fee, etc.
(iii)	Whether payment is made to the debit of party's account on due date without creating overdraft/debiting suspense, in case of deferred payment guarantee.
H	Foreign Exchange transactions-Verify
(i)	Recovery of charges as per HO Guidelines.
(ii)	Packing credit released, whether backed by LC or confirmed export order.
(iii)	Availability of ECGC cover and compliance with ECGC terms.
(iv)	Submission of statutory returns on export/ import transactions, like BEF statements, XOS, write off of export bills, etc. Follow up of outstanding export bills and exchange control copy of bill of entry.
(v)	Irregularities in opening of new accounts and operation in NRO, FCNR, NRE, EEFC, etc., and debits/credits entries permissible under the rules.

(vi)	Whether operations in FCRA accounts are as permitted by MHA and FCRA guidelines.
(vii)	Booking, utilization, extension and cancellation of forward contracts.
I	House Keeping -Verify
(i)	Exceptional transaction reports are generated and verified by branch staff as prescribed.
(ii)	Review of all balance sheet heads and outstanding entries in accounts, e.g., suspense, sundry and inter-bank accounts. Review of follow up of entries pending for reversal.
(iii)	Scrutiny of daily vouchers with more emphasis on high value transaction including high value expenses and debit entries in Suspense account.
(iv)	Debits in accounts where signatures are pending for scanning.
(v)	Whether records related to KYC/vouchers and other critical areas are sent to specific places like archival center, record room as per stipulated periodicity.
(vi)	Adherence to KYC/AML guidelines in opening fresh account and subsequent modifications of records and monitoring of transaction.
J	Verification of Merchant Banking Business-Verify
(i)	Whether the instructions given by the controlling branch are properly followed where the branch acts as a collecting branch for issue business.
(ii)	Whether daily collection position is advised to the controlling branch.
(iii)	Whether recovery of the commission/fees and out of pocket expenses as agreed with the respective companies and whether the competent authority has duly authorized any waiver or reduction of such charges.
(iv)	Whether the prescribed preventive vigilance measures are observed by the branch.
(v)	Where data entry or data processing work is entrusted to outside agencies, the competent authority duly approves these and the prescribed stamped indemnity has been obtained from such agencies.
(vi)	Whether dividend interest warrants/refund payment accounts of companies are funded prior to dispatch of the relative warrants by the companies and there is no misuse of the facility.

(vii)	Whether Claims for reimbursement of amounts of paid warrants received from paying branches are processed and debited to the concerned company's account promptly.
(viii)	Whether charge on security has been created, wherever debenture trustee activity is undertaken by bank.
K	Verification of Credit Card/Debit card –Verify
(i)	Application for the issue of credit card has been properly examined and record of issue of the same has been maintained.
(ii)	Whether overdraft/debits arising out of the use of credit cards are promptly recovered and informed to higher authorities.
(iii)	Whether undelivered credit cards are properly kept as security items and followed up with credit card department for further instructions.
(iv)	Physical verification of ATM cards, debit cards, credit cards, passwords and PINS, control over issue & delivery, safe keeping and custody at all the locations. Report loss of any such items.
L	Others –Verify
(i)	Compliance of provisions relating to Tax Deducted at Source, service tax, trade tax, other duties and taxes.
(ii)	Physical verification of inventory, control over issue of inventory, safe keeping and custody of security forms. Report any loss of such items.
(iii)	Physical verification of other deliverable items, control over issue, safe keeping and custody.
(iv)	Physical verification of Gold coins, control over issue, safe keeping and custody. Checking of Gold sale transactions.
(v)	Custody and movement of branch keys.
(vi)	Locker keys and locker operations-linking of FDR as security for locker/operation of locker/inoperative lockers/ nomination/other issues.
(vii)	Safe custody of branch documents like death claim cases, issuance of duplicate DD/PO/FDR, checking of indemnities, etc. and verification of documents executed during the period under audit.
(viii)	Reporting of frauds.

APPENDIX II

List of RBI Circulars and Master Directions (*Included in CD*)

EFFECTIVE CONCURRENT AUDIT

(i) Concurrent Audit System in Commercial Banks - Revision of RBI's Guidelines

RBI/2015-16/133 - DBS.CO.ARS.No. BC. 2/08.91.021/2015-16 dated July 16, 2015

(ii) Submission of Long Form Audit Report (LFAR) by Concurrent Auditors RBI/2014-15/626- DBS.CO.ARS.BC.8/08.91.001/2014-15 dated June 4, 2015

(iii) Master Circulars on Audit Systems issued by Department of Financial Services, Government of India

F. No. 7/124/2012-BOA dated September 26, 2012

(iv) Master Circular- Risk Based Supervision – Follow up of Risk Management Systems in Banks

RBI/2015-16/352- DBS.CO.PPD.10887/11.01.005/2015-16 dated March 31, 2016

(v) Master Circular- Information System Audit - A review of Policies and Practices

RBI/2004/191-DBS.CO.OSMOS.BC/ 11 /33.01.029/2003-04 dated April 30, 2004

KYC NORMS AND PMLA ACT, 2002

(i) Master Direction - Know Your Customer (KYC) Direction, 2016

RBI/DBR/2015-16/18- Master Direction

DBR.AML.BC.No.81/14.01.001/2015-16 dated 25.2.2016

(ii) Master Circular – Know Your Customer (KYC) norms / Anti-Money Laundering (AML) standards/Combating Financing of Terrorism (CFT)/Obligation of banks and financial institutions under PMLA, 2002

RBI/ 2015 – 16/42 - DBR.AML. BC. No. 15 /14.01.001/2015-16 dated July 1, 2015

(iii) Opening of Current Accounts by Banks - Need for Discipline RBI/2015-16/112 -DBR.Leg.BC.25./09.07.005/2015-16 dated July 2, 2015

(iv) Misuse of Banking Channels - Issue and Payment of Demand Drafts for ₹ 50,000/- and above

RBI/ 2011-12/135 - DBOD.BP.BC. No. 26 / 21.01.001/2011-12 dated August 1, 2011

(v) Issue of Demand Drafts for ₹ 20,000/- and above

RBI/ 2011-12/250 -DBOD.BP.BC. No. 49 / 21.01.001/2011-12 dated November 4, 2011

DILIGENCE REPORT FOR BANKS

(i) Lending under Consortium Arrangement/Multiple Banking Arrangements

RBI/2008-2009/183 - DBOD No. BP. BC.46/ 08.12.001/2008-09 dated September 19, 2008

(ii) Lending under Consortium Arrangement/Multiple Banking Arrangements

RBI/2008-2009/313 - DBOD.No. BP.BC.94 /08.12.001/2008-09 dated December 08, 2008

(iii) Lending under Consortium Arrangement/ Multiple Banking Arrangements RBI/2008-2009/379 - DBOD.No. BP.BC.110/08.12.001/2008-09 dated February 10, 2009

(iv) Second Quarter Review of Monetary Policy 2012-13 – Non-Performing Assets (NPAs) and Restructuring of Advances

RBI/2012-13/304 - DBOD. BP.BC.No. 62 /21.04.103/2012-13 dated November 21, 2012

(v) Transfer of Borrowal Accounts from One Bank to Another

RBI/2011-12/551 -DBOD.No.BP.BC- 104 /21.04.048/2011-12 dated May 10, 2012

LOANS AND ADVANCES

Financial Inclusion and Development

(i) Master Circular - Credit facilities to Scheduled Castes (SCs) & Scheduled Tribes (STs)

RBI/2015-16/60 - FIDD.CO.GSSD.BC.No 06/ 09.09.01/2015-16 dated July 01, 2015

(ii) Master Circular- Credit Facilities to Minority Communities

RBI/2015-16/64 - FIDD. GSSD. BC.No.05 /09.10.01/2015-16 dated July 1, 2015

(iii) Master Circular- Guidelines for relief measures by banks in areas affected by Natural calamities

RBI/2015-16/68 - FIDD. No. FSD. BC.01 /05.10.001/2015-16 dated July 01, 2015

(iv) Master Circular-Lead Bank Scheme

RBI/2015-16/48 -FIDD.CO.LBS.BC.No. 3 /02.01.001/2015-16 dated July 1, 2015

(v) Master Circular - Lending to Micro, Small & Medium Enterprises (MSME) Sector

RBI/2015-16/74 - FIDD.MSME &NFS.BC.No. 07/06.02.31/2015-16 dated July 1, 2015

(vi) Master Circular-Priority Sector Lending- Targets and Classification

RBI/2015-16/53 - FIDD.CO.Plan.BC.04/04.09.01/2015-16 dated July 1, 2015

(vii) Master Circular on SHG-Bank Linkage Programme

RBI/2015-16/29 - FIDD.FID.BC.No.02/12.01.033/ 2015-16 dated July 01, 2015

Other Master Circulars on Loans and Advances

(viii) Master Circular - Bank Finance to Non-Banking Financial Companies (NBFCs)

RBI/2015 -16/36 - DBR.BP.BC.No.5/21.04.172/2015-16 dated July 1, 2015

(ix) Master Circular on Credit Card, Debit Card and Rupee Denominated Co-branded Pre-paid Card Operations of Banks and Credit Card issuing NBFCs

RBI/2015-16/31- DBR.No.FSD.BC.18/24.01.009/2015-16 dated July 1, 2015

(x) Master Circular-Exposure Norms

RBI /2015-16/70- DBR.No.Dir.BC.12 /13.03.00/2015-16 dated July 1, 2015

(xi) Master Circular - Exposure Norms for Financial Institutions

RBI/2015-16/102 - DBR.FID.FIC.No.4/01.02.00/2015-16 dated July 1, 2015

(xii) Master Circular-Guarantees and Co-acceptances

RBI/2015-16/76- DBR. No. Dir. BC.11 /13.03.00/2015-16 dated July 1, 2015

(xiii) Master Circular - Housing Finance

RBI/2015-16/46- DBR.No.DIR.BC.13/08.12.001/2015-16dated July 1, 2015

(xiv) Master Circular - Interest Rates on Advances

RBI/2015-16/37- DBR.No.Dir.BC.9/13.03.00/2015-16 dated July 1, 2015

(xv) Master Circular Loans and Advances – Statutory and Other Restrictions RBI/2015-16 /95- DBR.No.Dir.BC.10/13.03.00/2015-16 dated July 1, 2015

(xvi) Master Circular- Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances

RBI/2015-16/101 - DBR.No.BP.BC.2/21.04.048/2015-16 dated July 1, 2015

(xvii) Master Circular on Willful Defaulters

RBI/2015-16/100 - DBR.No.CID.BC.22/20.16.003/2015-16 dated July 1, 2015

(xviii) Master Circular -Rupee / Foreign Currency Export Credit and Customer Service To Exporters

RBI/2015-16/47-DBR No.DIR.BC.14/ 04.02.002/ 2015-16 dated July 1, 2015

Other Circulars on Loans and Advances

(xix) Discount Rate for Computing Present Value of Future Cash Flows

RBI/2015-16/111 - DBR.No.BP.BC.27/21.04.048/2015-16 dated July 2, 2015

(xx) Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances – Credit Card Accounts

RBI/2015-16/126 - DBR.No.BP.BC.30/21.04.048/2015-16 dated July 16, 2015

(xxi) Revised Kisan Credit Card (KCC) Scheme

RBI/2011-12/553 - RPCD.FSD.BC.No.77/05.05.09/2011-12 dated May 11, 2012

(xxii) Revised Kisan Credit Card (KCC) Scheme

RBI/2012-13/162 -RPCD.FSD.BC.No. 23 /05.05.09/2012-13 dated August 7, 2012

(xxiii) Union Budget 2014-2015 Interest Subvention Scheme

RBI/2014-15/417 - FIDD.No.FSD.BC.48/05.04.02/2014-15 dated January 21, 2015

(xxiv) Union Budget – 2015-16 Interest Subvention Scheme

RBI/2014-15/557-FIDD.No.FSD.BC.53/05.04.02/2014-15 dated April 16, 2015

(xxv) Legal Audit of title documents in respect of large value loan accounts

RBI/ 2012-13/524 - DBS.FrMC.BC.No.7/23.04.001/2012-13 dated June 07, 2013

(xxvi) End use of funds- Monitoring

RBI/ 2010-11/368 - DBS.CO.PPD.BC.No. 5 /11.01.005/2010-11 dated January 14, 2011

(xxvii) Levy of foreclosure charges/pre-payment penalty on Floating Rate Term Loans

RBI/ 2013-14/582 - DBOD. Dir.BC.No. 110 /13.03.00/2013-14 dated May 7, 2014

(xxviii) Review of Prudential Guidelines - Revitalising Stressed Assets in the Economy

RBI/2015-16/330-DBR.BP.BC.No.82/ 21.04.132 / 2015-16 dated 25.2.2016

FOREX AND TRADE

(i) Master Circular – Memorandum of Instructions governing money changing activities

RBI/2015-16/92 -Master circular no.10/2015-16 dated July 01, 2015 (Updated on September 10, 2015)

(ii) Guidelines issued under Section 36(1)(a) of the Banking Regulation Act, 1949- Implementation of the provisions of Foreign Contribution (Regulation) Act, 2010

RBI/2015-16/35 -DBR.AML.BC.No.16/14.08.001/2015-16 dated July 1, 2015

(iii) Master Circular – Interest rates on Deposits held in FCNR (B) Accounts

RBI/2015-16/40 -DBR No.Dir.BC.8/13.03.00/2015-16 dated July 1,2015

(iv) Master Circular – Non-Resident Ordinary Rupee (NRO) Account

RBI/2015-16/78 -Master circular No.2/2015-16 dated July 1, 2015

(v) Master Circular – Miscellaneous Remittances from India-Facilities for Residents

RBI/2015-16/91 -Master Circular No.6/ 2015-16 dated July 1, 2015

(vi) Master Circular – Remittance Facilities for Non-Resident Indians/Persons of Indian Origin/Foreign Nationals

RBI/2015-16/80 -Master Circular no.8/2015-16 dated July 01, 2015

(vii) Export Factoring on non-recourse basis

RBI/2015-16/129 -A.P.(DIR Series) Circular No.5 dated July 16, 2015

(viii) Master Circular – Acquisition and Transfer of Immovable Property in India by NRIs/PIOs/Foreign Nationals of Non-Indian Origin.

RBI/2015-16/79-Master Circular No.4/2015-16 dated July 1, 2015

(ix) Master Circular – Memorandum of Instructions for Opening and Maintenance of Rupee/Foreign Currency Vostro Accounts of Non-resident Exchange Houses

RBI/2015-16/89 - Master Circular No.3/2015-16 dated July 01, 2015

(x) Master Circular – Import of Goods and Services

RBI/2015-16/82 -Master circular No.13/ 2015-16 dated July 01, 2015

(xi) Master Circular – Export of Goods and Services

RBI/2015-16/83 -Master Circular no.14/2015-16 dated July 01, 2015(Updated as on July 16, 2015)

(xii) Re-export of unsold rough diamonds from Special Notified Zones of Customs without Export Declaration Form (EDF) Formality

RBI/2015-16/110 -A.P.(DIR Series) Circular No.1 dated July 2, 2015

(xiii) Master Circular – Compounding of Contraventions under FEMA, 1999

RBI/2015-16/67 -Master Circular No.9/2015-16 dated July 01.2015

(xiv) Master Circular – Establishment of Liaison/Branch/ Project Offices in India by Foreign Entities

RBI/2015-16/54- Master Circular No.7/2015-16 dated July 01, 2015

(xv) Master Circular – Foreign Investment in India

RBI/2015-16/96- Master Circular No.15/2015-16 dated July 01, 2015 (Updated as on July 16, 2015)

(xvi) Master Circular – Direct Investment by Residents in Joint Venture (JV) /Wholly Owned Subsidiary (WOS) Abroad

RBI/2015-16/41 -Master Circular No.11/ 2015-16 dated July 01, 2015

(xvii) Master Circular – External Commercial Borrowings and Trade Credits

RBI/2015-16/33- Master Circular No.12/2015-16 dated July 01, 2015 (Updated as on September 11. 2015)

(xviii) Master Circular- Rupee / Foreign Currency Export Credit and Customer Service To Exporters

RBI/2015-16/47- DBR No.DIR.BC.14/04.02.002/2015-16 dated July 1, 2015

(xix) Master Circular- Liberalised Remittance Scheme of USD 25,000 for Resident Individuals

RBI/ 2004/39- A.P. (DIR Series) Circular No. 64 dated February 4, 2004

FRAUDS

(i) Frauds – Classification and Reporting

RBI/2015-16/75 - DBS.CO.CFMC.BC.No.1/ 23.04.001/2015-16 dated July 01, 2015.

(ii) Master Directions on Frauds – Classification and Reporting by commercial banks and select FIs

RBI/DBS/2016-17/28- DBS.CO.CFMC.BC.No.1/23.04.001/2016-17 dated July 1, 2016

CONCURRENT AUDIT PROCEDURES

A. Currency

(i) Master Circular – Detection and Impounding of Counterfeit Notes

RBI /2015-16/52 - DCM (FNVD) G- 4/16.01.05/2015-16 dated July 1, 2015

(iii) Master Circular – Levy of Penal Interest for Delayed Reporting/Wrong Reporting/Non-Reporting of Currency Chest Transactions and Inclusion of Ineligible Amounts in Currency Chest Balances

RBI/2015-16/49 - DCM (CC) No. G - 1 /03.35.01/2015-16 dated July 01, 2015

(iv) Master Circular – Facility for Exchange of Notes and Coins

RBI/2015-16/38 - DCM (NE) No. G - 2/08.07.18/2015-16 dated July 01, 2015

(v) Stapling of Note Packets - Removal

DBOD No Dir.BC.42/13.03.00/2001-02 dated November 7,2001

(vi) Clean Note Policy

RBI/ 2013-14/ 183- DCM (NPD) No. G-11 /09.39.000 /2013-14 dated August 14, 2013

(vii) Withdrawal of all old series of Banknotes issued prior to 2005

RBI/ 2013-14/467-DCM (Plg) No.G-17/3231/10.27.00/2013-14 dated January 23, 2014

(viii) Withdrawal of all old series of Banknotes issued prior to 2005

RBI/2013-14/509-DCM (Plg) No.G- 19/3880/10.27.00/2013-14 dated March 03, 2014

(ix) Withdrawal of all old series of Banknotes issued prior to 2005

RBI/2014-15/650 - DCM (Plg) No.G-15/5486/10.27.00/2014-15 dated June 26, 2015

B. ATM/WLA(White Label ATM)

(i) Disclosure of customer complaints and unreconciled balances on account of ATM transactions

RBI/2013-14/218 -DBOD.BP.BC.No.49/21.04.018/2013-14 dated September 3, 2013

(ii) White Label ATMs (WLAs) in India - Guidelines

RBI/2011-12/612 - DPSS.CO.PD. No. 2298 / 02.10.002 / 2011-2012 dated June 20, 2012

(iii) White Label ATMs (WLAs) in India – Clarification on Cash Handling

RBI/ 2013-14/ 372 -DPSS.CO.PD. No. 1088 / 02.10.003 / 2013-14 dated November 14, 2013

(iv) White Label ATMs (WLAs) in India - Guidelines

RBI/2014-15/338 - DPSS.CO.PD. No. 1025/02.10.003/2014-2015 dated December 5, 2014

C. Government Business

(i) Master Circular on Appointment and Delisting of Brokers, and Payment of Brokerage on Relief/Savings Bonds

RBI/2015-16/51- IDMD.CDD.No.5984 /13.01.299/2015-16 dated July 01, 2015

(ii) Master Circular -Collection of Direct Taxes- OLTAS RBI/2015-16/90- DGBA.GAD.No.3/42.01.034/2015-16 dated July 1, 2015

(iii) Master Circular on Nomination Facility for Relief/Saving Bonds RBI/2015-16/50 - IDMD.CDD. No.5983 /13.01.299/2015-16 dated July 01, 2015

(iv) Master Circular - Disbursement of Government Pension by Agency Banks

RBI/2015-16/63 - DGBA.GAD.No.H-1/31.05.001/2015-16 dated July 1, 2015

(v) Master Circular on Conduct of Government Business by Agency Banks - Payment of Agency Commission

RBI/2015-16/81 - DGBA.GAD.No.2/31.12.010/2015-16 dated July 1, 2015 (Updated as on August 13, 2015)

D. Deposits

(i) Master circular on Interest Rates on Rupee Deposits held in Domestic,(Ordinarily Non- Resident NRO and Non- Resident (External) NRE Accounts

RBI /2015-16/39- DBR.No.Dir.BC. 7/13.03.00/2015-16 dated July 1, 2015

(ii) Repayment of Term/Fixed Deposits in banks

RBI/2011-12/248-DBOD No. Leg BC 46 /09.07.005/2011-12 dated November 4, 2011

(iii) Premature Repayment of Term/Fixed Deposits in banks with "Either or Survivor" or "Former or Survivor" mandate – Clarification

RBI/ 2012-13/168- DBOD No. Leg. BC. 37 /09.07.005/2012-13 dated August 16, 2012

(iv) Opening of Bank Accounts in the Names of Minors

RBI/ 2013-14/ 581 - DBOD. No. Leg. BC. 108 /09.07.005/2013-14 dated May 6, 2014

(v) Unclaimed Deposits / Inoperative Accounts in banks

RBI/2008-09/138 - DBOD. No. Leg. BC. 34 /09.07.005/2008-09 dated August 22, 2008

(vi) Inoperative Accounts

RBI/ 2009-10/202 - DBOD.Leg. No.BC. 55 /09.07.005 /2009-10 dated October 30, 2009

(vii) Levy of penal charges on non-maintenance of minimum balances in inoperative Accounts

RBI/2013-14/580 - DBOD. Dir.BC.No. 109 /13.03.00/2013-14 dated May 6, 2014

(viii) Inoperative Accounts

RBI /2014-15/200 -DBOD.No. Leg. BC. 36 /09.07.005/2014-15 dated Sept 1, 2014

(ix) The Banking Companies (Nomination) Rules, 1985 – Clarifications

RBI/ 2011-12/469 - DBOD.No. Leg.BC. 89/ 09.07.005/2011-12 dated March 26, 2012

(x) Legal Guardianship Certificates Issued under the Mental Health Act, 1987and National Trust for the Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities Act, 1999

RBI/2013-14/ 444 -DBOD. No. Leg. BC. 84 /09.07.005/2013-14 dated January 21, 2014

E. Circular on other banking procedures

(i) Acknowledgement by banks at the time of submission of Form 15G / 15H

RBI/2012-13/516-DBOD.No.Leg.BC.100 /09.07.005/2012-13 dated May 31, 2013

(ii) Standardisation and Enhancement of Security Features in Cheque Forms

RBI/ 2009-10/323-DPSS.CO.CHD.No. 1832 / 04.07.05 / 2009-10 dated February 22, 2010

(iii) Standardisation and Enhancement of Security Features in Cheque Forms

RBI 2009-10/503-DPSS. CO. CHD. No. 2806 / 04.07.05 / 2009-10 dated June 22, 2010

(iv) Standardization and Enhancement of Security Features in Cheque Forms/Migrating to CTS 2010 standards

RBI/ 2013-14/141-DPSS.CO.CHD.No./133 / 04.07.05 / 2013-14 dated July 16, 2013

(v) Payment of Cheques/Drafts/Pay Orders/Banker's Cheques

RBI/ 2011-12/251- DBOD.AML BC.No.47/14.01.001/2011-12 dated November 4, 2011

(vi) Cheque related fraud cases - preventive measures

RBI/ 2014-15/294- DBS.CFMC.BC.No. 006/23.04.001/2014-15 dated November 5, 2014

(vii) Settlement of claims in respect of deceased depositors – Simplification of Procedure

RBI/2004-05/490- DBOD.No.leg. BC.95 /09.07.005/2004-05 dated June 9, 0025

(viii) Extension of Safe Deposit Locker / Safe CustodyArticle Facility and Access to Safe Deposit Lockers /Return of Safe Custody Articles by banks

RBI/2006-2007/325- DBOD.No.Leg.BC.78 /09.07.005/2006-07 dated April 17, 2007

(ix) Levy of interest on clearing-related overdraft extended by Clearing House managing banks for settling clearing obligations of member banks

RBI/2009-10/452 - DPSS.CO (CHD) No. 2387/03.06.01/2009-2010 dated May 6, 2010

(x) Master Circular on Customer Service in Banks RBI/2015-16/59- DBR No.Leg.BC. 21/09.07.006/2015-16 dated July 1, 2015

F. Payment and Settlement System

(i) Master Circular – Mobile Banking transactions in India – Operative Guidelines for Banks

RBI/ 2015-16/65 -DPSS.CO.PD.Mobile Banking.No.1/02.23.001/2015-16 dated July 1, 2015

(ii) Master Circular – Policy Guidelines on Issuance and Operation of Pre-paid Payment Instruments in India

RBI/2015-2016/66-DPSS.CO.PD.PPI.No. 2/02.14.006/2015-16 dated July 01, 2015

G. Branch Licensing

(i) Master Circular on Branch Licensing

RBI/2015-16/10 - DBR.CO.RRB.BL.BC.No. 17 /31.01.002 /2015-16 dated July 1, 2015

BASEL CAPITAL REGULATORY REQUIREMENTS

(i) Master Circular- Basel III Capital Regulations RBI/2015-16/58-DBR.No.BP.BC.1/21.06.201/2015-16 dated July 1, 2015

(ii) Master Circular - Prudential Guidelines on Capital Adequacy and Market Discipline-New Capital Adequacy Framework (NCAF)

RBI/2015-16/85 - DBR.No.BP.BC.4./21.06.001/2015-16 dated July 1, 2015

(iii) Master Circular -Prudential Norms on Capital Adequacy - Basel I Framework
RBI/2015-16/86- DBR.No.BP.BC. 3/21.01.002/2015-16 dated July 1, 2015

TREASURY AND INVESTMENT

(i) Master Circular- Capital Adequacy Standards and Risk Management Guidelines for Standalone Primary Dealers

RBI/2015-16/106 - DNBR (PD) CC. No.062/03.10.119/2015-16 dated July 01, 2015

(ii) Master Circular- Operational Guideline for Primary Dealers

RBI/2015-16/34 - IDMD.PDRD.01 /03.64.00/2015-16 dated July 1, 2015

(iii) Master Circular- Prudential Guidelines for the Primary Dealers in Government Securities Market

RBI/2015-16/105- DNBR (PD) CC. No. 063/03.10.119/2015-16 dated July 1, 2015

(iv) Master Circular on Call/Notice Money Market Operations

RBI/2015-16/55 - FMRD.DIRD. 01 /14.01.001/2015-16 dated July 1, 2015

(v) Master Circular - Guidelines for Issue of Certificates of Deposit

RBI/2015-16/57 - FMRD.DIRD. 03 /14.01.003/2015-16 dated July 1, 2015

(vi) Master Circular - Guidelines for Issue of Commercial Paper

RBI/2015-16/56 - FMRD.DIRD.02/14.01.002/2015-16 dated July 1, 2015

(vii) Master Circular - Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR)

RBI/2015-16/98- DBR.No.Ret.BC.24/12.01.001/2015-16 dated July 1, 2015

(viii) Master circular- Para-banking Activities

RBI/2015-16/30- DBR.No.FSD.BC.19/24.01.001/2015-16 dated July 1, 2015

(ix) Master Circular- Prudential Norms for Classification, Valuation and Operation of Investment Portfolio by Banks

RBI/2015-16/97 -DBR No BP.BC.6 /21.04.141/2015-16 dated July 1, 2015

(x) Master Circular -Prudential Norms for Classification, Valuation and Operation of Investment Portfolio by FIs

RBI/2015-16/104 -DBR.No.FID.FIC.3/01.02.00/2015-16 dated July 1, 2015

(xi) Master Circular - Resource Raising Norms for Financial Institutions

RBI/2015-16/69 - DBR.No.FID.FIC.1/01.02.00/2015-16 dated July 1, 2015

DISCLOSURE NORMS

(i) Master Circular- Disclosure Norms for Financial Institutions

RBI/2015-16/103- DBR.No.FID.FIC.2/01.02.00/2015-16 dated July 1, 2015

(ii) Master Circular - Disclosure in Financial Statements - 'Notes to Accounts

RBI/2015-16/99 DBR.BP.BC No.23 /21.04.018/2015-16 dated July 1, 2015

MASTER CIRCULAR ON COOPERATIVE BANKS

(i) Master Circular on Area of Operation, Branch Authorisation Policy, Opening/ Up-gradation of Extension Counters, ATMs and Shifting/Splitting/Closure of Offices

RBI/2015-16/62 -DCBR.LS.(PCB)MC.No.16/07.01.000/2015-16 dated July 1, 2015

(ii) Master Circulars on Board Of Director-UCBs

RBI/2015-16/2 -DCBR.BPD (PCB/RCB) Cir.No.2/14.01.062/2015-16 dated July 1, 2015

(iii) Master Circular on Frauds- Classification and Reporting

RBI/2015-16/1 -DCBR.CO.BPD.MC.No.1/12.05.001/2015-16 dated July 1, 2015

(iv) Master Circular on Customer Service-UCBs

RBI/2015-16/61 -DCBR.CO.BPD.(PCB).MC.No.15/12.05.001/2015-16 dated July 1, 2015

(v) Master Circular-Exposure Norms and Statutory /other Restrictions-UCBs

RBI/2015-16/45 -DCBR.CO.BPD. (PCB) MC No.13/13.05.000/2015-16 dated July 1, 2015

(vi) Master Circular-Finance for Housing Schemes - UCBs RBI/2015-16/07 - DCBR.BPD. (PCB) MC No.9/09.22.010/2015-16 dated July 1, 2015

(vii) Master Circular- Guarantees, Co-Acceptances & Letters of Credit - UCBs

RBI/2015-16/6 - DCBR.BPD. (PCB) MC No.8/09.27.000/2015-16 dated July 1, 2015

(viii) Master Circular- Income Recognition, Asset Classification, Provisioning and Other Related Matters – UCBs

RBI/2015-16/44 - DCBR.BPD. (PCB) MC No.12/09.14.000/2015-16 dated July 1, 2015

(xi) Master Circular on Inspection & Audit Systems in Primary (Urban) Co-operative Banks

RBI/2015-16/3- DCBR.CO.BPD.(PCB).MC.No. 3/12.05.001/2015-16 dated July 1, 2015

(ix) Master Circular- Interest Rates on Rupee Deposits – Primary (Urban) Co-operative Banks

RBI/2015-16/32 - DCBR.BPD (PCB) MC.No.7/13.01.000/2015-16 dated July 1, 2015

(x) Master Circular on Investments by Primary (Urban) Co-operative Banks

RBI/2015-16/43 - DCBR. BPD (PCB).MC.No. 4/16.20.000/2015-16 dated July 1, 2015

(xi) Master Circular on Maintenance of Deposit Accounts-Primary (Urban) Co-operative Banks

RBI/2015-16/5 - DCBR.BPD.(PCB). MC.No: 6/13.01.000/2015-16 dated July 1, 2015

(xii) Master Circular- Management of Advances - UCBs

RBI/2015-16/77 - DCBR.BPD.(PCB) MC No. 14 /13.05.000/2015-16 dated July 1, 2015

(xiii) Master Circular- Prudential Norms on Capital Adequacy- UCBs RBI/2015-16/9- DCBR.BPD.(PCB). MC.No.10 /09.18.201/2015-16 dated July 1, 2015

(xiv) Master Circular- Priority Sector Lending - UCBs

RBI/2015-16/8 - DCBR.BPD.(PCB). MC.No: 11 /09.09.001/2015-16 dated July 1, 2015

(xvi) Master Circular on Maintenance of Statutory Reserves - Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR) by Primary (Urban) Co-operative Banks

RBI/2015-16/4 - DCBR.BPD.(PCB). MC.No.5/12.03.000/2015-16 dated July 1, 2015

(Source: Reserve Bank of India)

Abbreviations

ACB	Audit Committee of Board of Directors
AMC	Asset Management Company
ATM	Automated Teller Machine
BRs	Bank Receipts
CBS	Core Banking Solutions
Cr	Credit
CFT	Combating the Financing of Terrorism
DD	Demand Draft
DDP	Demand Draft Payable
DFS	Department of Financial Services
DICGC	Deposit Insurance and Credit Guarantee Corporation
Dr	Debit
ECB	External Commercial Borrowings
ECGC	Export Credit Guarantee Corporation
ECS	Electronic Clearing System
EFT	Electronic Funds Transfer
EMI	Equated Monthly Instalment
FCRA	Foreign Contribution Regulation Act
FDI	Foreign Direct Investment
FEDAI	Foreign Exchange Dealers' Association of India
FEMA	Foreign Exchange Management Act
FERA	Foreign Exchange Regulation Act
FOREX	Foreign Exchange
GL	General Ledger
HO	Head Office
IBA	Indian Banks' Association
ICAI	Institute of Chartered Accountants of India
IS	Information System
KYC	Know Your Customer

LC	Letter of Credit
LG	Letter of Guarantee
MICR	Magnetic Ink Character Recognition
NABARD	National Bank for Agriculture and Rural Development
NEFT	National Electronic Funds Transfer
PAN	Permanent Account Number
PMLA	Prevention of Money Laundering Act, 2002
RRB	Regional Rural Bank
RTGS	Real-time Gross Settlement System
SBI	State Bank of India
SGL	Subsidiary General Ledger
SIAs	Standards on Internal Audit issued by the Internal Audit Standards Board of the ICAI
SIDBI	Small Industries Development Bank of India
SLR	Statutory Liquidity Ratio
SSI	Small Scale Industries
STR	Suspicious Transaction Report
TIN	Tax Information Network

Notes